CAPITAL FARM CREDIT

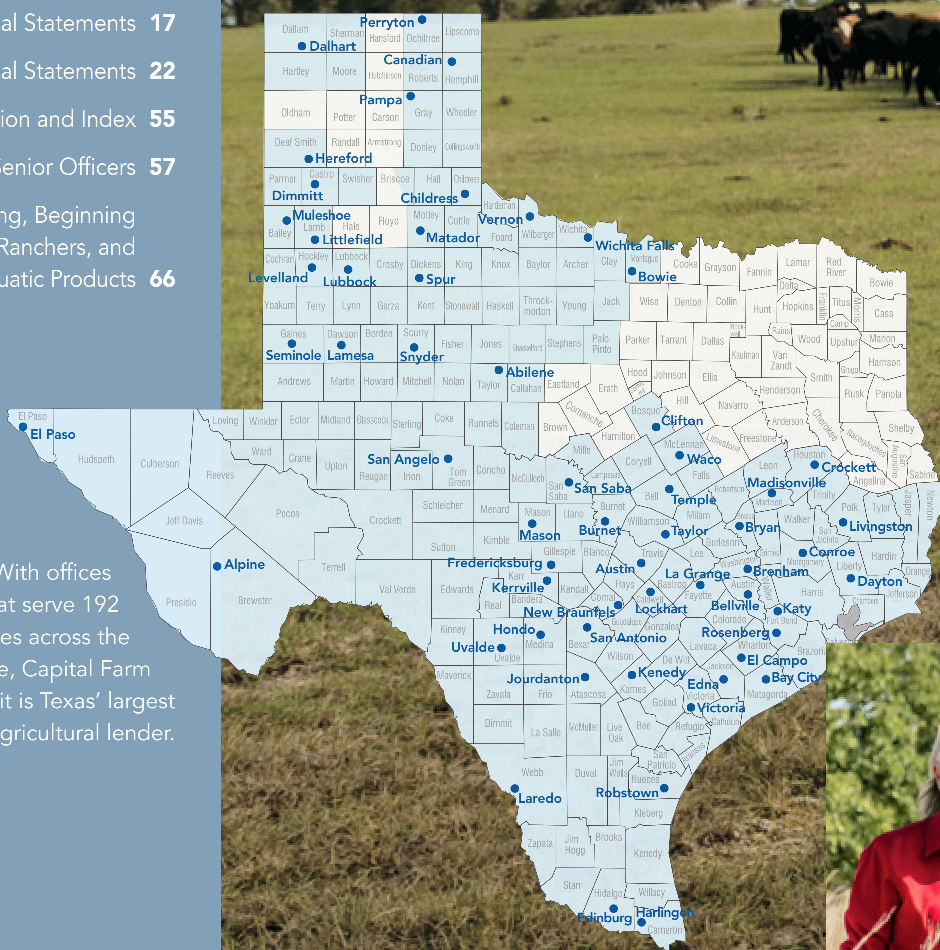
Together we're *better.*

# Here for *you.*

Annual Report 2022

# *Contents*






With offices that serve 192 counties across the state, Capital Farm Credit is Texas' largest agricultural lender.

**Birdwell and Clark Ranch**
Henrietta

capitalfarmcredit.com
877.944.5500
NMLS493828

# Here for *you.*

Capital Farm Credit is a lending and financial services cooperative serving rural Texas — for those who love and tend to the land — ensuring agriculture thrives. We've had the same mission since Texas agricultural producers formed our cooperative more than a century ago. We're here to empower farmers, ranchers, homebuyers and land seekers with customized financing and unrivaled market knowledge so they can lead the life they envision.

Today we're more than 23,000 members strong and growing. These agricultural producers and rural homeowners are more than customers. They also own this lending cooperative and share in its success.

While we saw our growth slow slightly in 2022, it was still an incredibly productive year, and we have our members to thank for that. We look forward to our continued success together.

CAPITAL FARM CREDIT

**Abianne Falla**
Cat Spring


**Hylio Inc.**
Richmond

**Manuel Macias**
Brownfield

# Our *milestones*

*The milestones our association reaches every year are a direct result of the steps we take to ensure the livelihood of our members and our employees. Together, we thrive no matter the uncontrollable circumstances in our world because of our vision to help each other succeed. Looking back at the previous year, we can find a road map of achievements and accomplishments with a common goal of being here for one another.*

## Getting closer to you


New Seminole branch office

No matter where you are in Texas, you often find a Capital Farm Credit office in your backyard. In 2022, we unveiled new office locations in Katy, New Braunfels and Seminole to better serve customers across Texas.

However, customers don't have to make the journey to an office in order to receive our top-notch financial services. We constantly upgrade our virtual technology so we can serve you efficiently and securely, both in person and online.

Our Ag Banking Online services are available by visiting CapitalFarmCredit.com/ABOL.

## Winning an award for innovation

At Capital Farm Credit, we always strive to provide the best experience for our customers. In response to the pandemic and increased interest in digital accessibility, we enhanced and expanded our capabilities through the Nintex Process Platform to provide workflow solutions and streamline integration with existing software systems and customer portals.

These innovative efforts led to Capital Farm Credit's recognition as a 2022 Nintex Solution Innovation Award winner.

## Partnership that pays

Cooperative returns effectively lower the cost of doing business for farmers, ranchers and rural property owners, and sharing our earnings is the highlight of what we are honored to do as a cooperative.

In March 2022, Capital Farm Credit returned $108.1 million in cash patronage to our borrowers. Our board of directors also approved a $59.7 million cash retirement of the remainder of the allocated equities issued in 2013, which was paid in November. This makes the total cash distributions returned to our members $167.8 million in 2022.


Since 2006, we've declared more than $2.2 billion of the association's net income in the form of cash payments and allocated equity through our cooperative returns program. That represents more than 90% of our earnings.

## Completing the conversion

With the help of many dedicated Capital Farm Credit and Farm Credit Bank of Texas employees, we successfully converted to using FarmView this summer. This enhancement in lending technology brings us closer to our customers throughout the loan process. It is our hope that this transition allows us to continue to give our customers the best experience possible.

## Establishing the Rural 1st® partnership

To discover new ways to serve our customers, we built upon our knowledge of being your trusted advisor. Capital Farm Credit partnered with Rural 1st to bring Texas customers new rural home lending solutions.

Rural 1st has more than 100 years of experience helping rural residents achieve their country living dreams. This expertise creates further opportunities for Capital Farm Credit to be the partner of choice for rural lending in Texas.

Through this collaboration, Capital Farm Credit is better developing its current home lending department and further enhancing the customer experience. Texas customers now have access to a variety of Rural 1st products, including new home, construction, lot or home equity loans that meet the unique needs of rural financing.

## Securing a strong future

Texas is constantly changing. The way we do business is evolving. However, our agricultural roots remain the same. Knowing our customers is our priority. To better understand the needs and expectations of our valued customers, we worked with Aimpoint Research to conduct a multidimensional, predictive research study known as Farmer of the Future. This study provided insight into the future of production agriculture and the evolving consumer markets.

We hope to use the results of this research to increase customer satisfaction across all of our Capital Farm Credit locations and continue to faithfully serve our members for years to come.

## Unveiling paid parental leave

The success of Capital Farm Credit is built on our people. In 2022, we announced new parental leave for eligible employees and began providing up to eight weeks of paid leave for the birth, adoption or foster care of a child. We continue to seek new ways to provide our staff with the resources they need to flourish at home and in the workplace for the good of our Capital Farm Credit family and our members.

## Coming together as a CFC family

In July, Capital Farm Credit proudly hosted over 600 employees in San Marcos, Texas, for our Summer Breakaway event to rediscover our mission in our daily operations. During the sessions, employees were given the opportunity to reconnect, renew and recharge alongside their CFC family. In addition, the executive management team shared the association's strategic direction for the next three to five years. What we do as a team affects our members and rural Texas.

From the start of the year to closing a chapter on many milestones, our approach has kept you in mind. How can we better serve those who impact not only Texas, but different sectors of the world. Agriculture binds us all together. Together, we collaborate, we empower each other, and we find solutions to our greatest challenges in the industry. After a long day working cattle or harvesting crops, we're your friend. We're your family. We're here for you.

# Supporting ag *and* rural communities

## Wildfire relief

In response to devastating wildfire outbreaks across Texas in 2022, Capital Farm Credit partnered with other Farm Credit institutions to pledge a combined $162,500 to support the Texas and Southwestern Cattle Raisers Association and rural fire departments.

## Investing in the future

In keeping with our mission to sustain the future of agriculture and rural communities, last fall we partnered with the Texas A&M AgriLife Extension Service and Texas 4-H to fund the Norman Borlaug Youth in Agriculture Program. This new program encourages a community of youth leaders to resolve the challenges facing global food and fiber production.

It goes beyond traditional rural ag programs by bringing together students from rural and urban areas and challenging them to solve ag industry issues.

## Scholarship programs


Young people are our future, and we are honored to support their academic careers as a part of our mission to support agriculture and rural communities. In 2022 we awarded more than $140,000 in scholarships to students across Texas.

We also launched a new statewide scholarship contest for agricultural high school seniors. The Ag Student of the Week Program recognizes 10 students per week from each of our chartered regions. At the end of the school year, one honoree from each region will receive a scholarship.

## Plains market visit


In September, members of the leadership team visited Lubbock for several days. Activities included visits to several customers for a hands-on look at some of the incredible operations our borrowers have. We were able to see firsthand how some of our Capital Farm Credit members are positively impacting agriculture.

# CEO *message*

Dear Stockholders:

It seems like only yesterday that we began our second year together, ready to see what the next 12 months would have in store for Texas and all of us who call this great state home.

For our association, 2022 was a year of execution. It's the term I used repeatedly across our leadership channels and throughout our organization. During this time last year, I recall explaining to our team how a focus on execution would be the only way to successfully accomplish our ongoing initiatives. As a team, we found ourselves in a position directing new IT systems, record levels of loan volumes and the impacts of an unsteady economy, all while navigating a post-pandemic workplace with the goal to continue functioning at a superior level for our customers.

With 2023 now underway, I look back at our accomplishments in 2022 and see how successful we were at understanding execution. We remain in a very strong position as an association. After two years of record loan growth, hiring 200-plus team members and battling a global pandemic, we are finally able to focus on the things that matter most — our people and our customers.

We are positioned well for what lies ahead of us in 2023. We unveiled our Winning Combination last year, which is the board's long-term strategy focused on our customers, performance and culture. That strategy is supported by initiatives that will guide us into the future, growing as an organization and continuing to develop our exceptional customer service as your trusted advisor.

Amid all the changes in our world and the advancements we've made as an association, one thing remains the same. We are still in the business of people. We still remain committed to serving the full breadth of agriculture, understanding the role we play in helping sustain rural Texas. We are a cooperative. Our patronage program is one of the strongest in the nation, having returned more than 90% of our earnings to our members since 2006.

Thank you for putting your trust in Capital Farm Credit. We look forward to helping you achieve your goals and dreams. Together, we're better. We're here for you.

Jeff Norte
Chief Executive Officer

*A message from CEO Jeff Norte*

SCAN ME

## REPORT OF MANAGEMENT

The consolidated financial statements of Capital Farm Credit, ACA (association) are prepared by management, who is responsible for the statements' integrity and objectivity, including amounts that must necessarily be based on judgments and estimates. The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America. Other financial information included in the annual report is consistent with that in the consolidated financial statements.

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

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

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

Jeff Norte, Chief Executive Officer
*March 9, 2023*

John Malazzo, Chairman, Board of Directors
*March 9, 2023*

Sally Lawson, Chief Financial Officer
*March 9, 2023*

## REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The association's chief executive officer and chief financial officer 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 (1) designed by, or under the supervision of, the association's principal executives and principal financial officers or persons performing similar functions; (2) effected by its board of directors, management and other personnel; and (3) monitored for adherence to by the board's audit committee through the association's internal audit staff and internal credit reviewers 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 consolidated 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, 2022. In making the assessment, management used the framework in Internal Control — Integrated Framework, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the association concluded that as of December 31, 2022, 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 internal control over financial reporting as of December 31, 2022. A review of the assessment performed was reported to the association's audit committee.

J Norte

Jeff Norte, Chief Executive Officer
*March 9, 2023*

Sally Lawson

Sally Lawson, Chief Financial Officer
*March 9, 2023*

## REPORT OF AUDIT COMMITTEE

The audit committee (committee) is composed of six directors of Capital Farm Credit, ACA (the association). In 2022, the committee met five times. The committee oversees the scope of the association's system of internal controls and procedures and the adequacy of management's action with respect to recommendations arising from those auditing activities. The committee's approved responsibilities are described more fully in the Audit Committee Charter, which is available on request or on the association's website. The committee approved the appointment of PricewaterhouseCoopers LLP (PwC) for 2022.

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

In this context, the committee reviewed and discussed the association's audited consolidated financial statements for the year ended December 31, 2022 (audited consolidated financial statements), with management and PwC. The committee also reviews with PwC the matters required to be discussed by authoritative guidance, "The Auditor's Communication With Those Charged With Governance," and both PwC and the association's internal auditors directly provide reports on significant matters to the committee.

The committee discussed with PwC its independence from Capital Farm Credit, ACA. The committee also reviewed the nonaudit services provided by PwC and concluded that these services were not incompatible with maintaining the independent accountant's independence. The committee has discussed with management and PwC other matters and received assurances from them as the committee deemed appropriate.

Based on the foregoing review and discussions and relying thereon, the committee recommended that the board of directors include the audited consolidated financial statements in the association's Annual Report to Stockholders for the year ended December 31, 2022.

Sharleen Walkoviak, Chair

Additional Members: Terry McAlister
Kenton Kimball
Ronnie Riddle
Dale Crenwelge
Jim Brock

*March 9, 2023*

**CAPITAL FARM CREDIT, ACA**
**FIVE-YEAR SUMMARY OF SELECTED CONSOLIDATED FINANCIAL DATA**
**(unaudited)**
**(dollars in thousands)**

| | December 31, | | | | |
|---|---|---|---|---|---|
| | **2022** | 2021 | 2020 | 2019 | 2018 |
| **Balance Sheet Data** | | | | | |
| Assets | | | | | |
| Loans | **$ 11,487,825** | $ 10,456,511 | $ 8,684,131 | $ 7,822,838 | $ 7,393,006 |
| Less: Allowance for losses | **(21,386)** | (22,996) | (31,592) | (30,798) | (25,495) |
| Net Loans | **11,466,439** | 10,433,515 | 8,652,539 | 7,792,040 | 7,367,511 |
| Investment -- held-to-maturity | **1,496** | 1,952 | 2,582 | 3,418 | 4,388 |
| Investment in and receivable from the Bank: | **191,460** | 181,041 | 161,379 | 154,485 | 147,288 |
| Other property owned, net | **2,924** | 927 | 601 | 859 | 972 |
| Other assets | **179,911** | 134,432 | 126,539 | 135,177 | 119,297 |
| Total assets | **$ 11,842,230** | $ 10,751,867 | $ 8,943,640 | $ 8,085,978 | $ 7,639,456 |
| Liabilities | | | | | |
| Obligations with maturities of one year or less | **$ 221,235** | $ 224,973 | $ 196,972 | $ 172,634 | $ 168,172 |
| Obligations with maturities greater than one year | **9,892,648** | 8,893,589 | 7,395,111 | 6,629,186 | 6,239,046 |
| Total liabilities | **10,113,883** | 9,118,562 | 7,592,083 | 6,801,820 | 6,407,218 |
| Members' Equity | | | | | |
| Capital stock and participation certificates | **$ 28,337** | $ 28,410 | $ 27,043 | $ 25,980 | $ 25,804 |
| Preferred Stock | **200,000** | 200,000 | - | - | - |
| Non-qualified allocated retained earnings | **885,831** | 803,147 | 737,454 | 674,877 | 624,839 |
| Unallocated retained earnings | **610,986** | 604,705 | 590,617 | 586,224 | 581,674 |
| Accumulated other comprehensive income (loss) | **3,193** | (2,957) | (3,557) | (2,923) | (79) |
| Total members' equity | **1,728,347** | 1,633,305 | 1,351,557 | 1,284,158 | 1,232,238 |
| Total liabilities and members' equity | **$ 11,842,230** | $ 10,751,867 | $ 8,943,640 | $ 8,085,978 | $ 7,639,456 |
| | Year Ended December 31, | | | | |
| **Statement of Income Data** | | | | | |
| Net interest income | **$ 322,799** | $ 280,400 | $ 247,641 | $ 235,013 | $ 234,723 |
| Reversal (provision for) of credit losses | **1,003** | 9,198 | (582) | (8,101) | 3,469 |
| Income from the Bank | **71,109** | 59,185 | 48,940 | 40,403 | 35,041 |
| Other noninterest income | **23,092** | 25,888 | 22,431 | 14,794 | 15,293 |
| Noninterest expense | **(131,695)** | (112,908) | (98,172) | (101,099) | (98,676) |
| Benefit from (provision for) income taxes | **1** | (50) | - | (5) | 1 |
| Net income | **$ 286,309** | $ 261,713 | $ 220,258 | $ 181,005 | $ 189,851 |
| **Key Financial Ratios for the Year** | | | | | |
| Return on average assets | 2.5% | 2.7% | 2.6% | 2.3% | 2.5% |
| Return on average members' equity | 16.4% | 15.9% | 16.7% | 14.4% | 15.8% |
| Net interest margin as a percentage of average earning assets | 2.9% | 3.0% | 3.0% | 3.1% | 3.2% |
| Net charge-offs (recoveries) as a percentage of average loans | 0.00% | 0.0% | 0.0% | 0.0% | 0.0% |

**CAPITAL FARM CREDIT, ACA**
**FIVE-YEAR SUMMARY OF SELECTED CONSOLIDATED FINANCIAL DATA**
**(unaudited)**
**(dollars in thousands)**

| | December 31, | | | | |
|---|---|---|---|---|---|
| | **2022** | **2021** | **2020** | **2019** | **2018** |
| **Key Financial Ratios at Year End *** | | | | | |
| Members' equity as a percentage of total assets | 14.6% | 15.2% | 15.1% | 15.9% | 16.1% |
| Debt as a percentage of members' equity | 585.2% | 558.3% | 561.7% | 529.7% | 520.0% |
| Allowance for loan losses as a percentage of loans | 0.2% | 0.2% | 0.4% | 0.4% | 0.3% |
| Common Equity tier 1 ratio | 11.5% | 12.4% | 14.0% | 14.6% | 14.3% |
| Tier 1 capital ratio | 13.1% | 14.3% | 14.0% | 14.6% | 14.3% |
| Total capital ratio | 13.3% | 14.5% | 14.4% | 15.0% | 15.1% |
| Permanent capital ratio | 13.1% | 14.3% | 14.1% | 14.7% | 14.8% |
| Tier 1 leverage ratio | 13.9% | 15.0% | 14.7% | 15.2% | 14.8% |
| UREE leverage ratio | 5.4% | 7.3% | 8.4% | 8.9% | 9.5% |
| **Net Income Distribution/Allocation** | | | | | |
| Cash patronage paid | $ 108,069 | $ 98,280 | $ 88,550 | $ 87,543 | $ 77,506 |
| Cash retirement of nonqualified written notice of allocation | 59,747 | 60,000 | 55,000 | 38,206 | 50,000 |
| Nonqualified notices of allocation | 142,433 | 125,700 | 117,585 | 87,987 | 97,044 |
| Preferred stock dividends paid | 10,000 | 9,056 | - | - | - |

*Effective January 1, 2017, the Farm Credit Administration implemented new capital ratios. The association's ratios remained well above the regulatory minimums, including the conservation and leverage buffers at December 31, 2022. For more information, see Note 11 in the accompanying consolidated financial statements, "Members Equity," included in this annual report. The full amount of the association's Class B preferred stock is included in the permanent capital, tier 1 capital and total capital.

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (ALL DOLLAR AMOUNTS IN THOUSANDS)

The following commentary explains management's assessment of the principal aspects of the consolidated financial condition and results of operations of Capital Farm Credit, ACA, including its wholly owned subsidiaries, Capital Farm Credit, PCA and Capital Farm Credit, FLCA (collectively referred to as the association) for the years ended December 31, 2022, 2021 and 2020, and should be read in conjunction with the accompanying consolidated financial statements. The accompanying financial statements were prepared under the oversight of the association's audit committee.

**Forward-Looking Information:**

This annual report 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 the association's control. The association is impacted by factors that would impact any agricultural real estate lender. These risks and uncertainties include but are not limited to:

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

**Commodity Review and Economic Outlook:**

Capital Farm Credit is the largest agricultural lender headquartered in Texas, with a footprint that includes 192 of the 254 counties. This allows for not only geographic, but also commodity diversity, reducing overall concentration risk to the association. Capital Farm Credit meets the needs of both full-time and part-time producers as well as agribusinesses in many industry sectors by providing an array of loan products and services to its members. The association has seen significant growth balanced across these sectors of the portfolio in the past three years, culminating in $3.7 billion, or 46.8 percent, increase in loan volume.

The Texas economy remained strong throughout the year, with job growth outpacing the U.S. 3.5 percent to 3.2 percent in 2022. The majority of the job growth came in the oil and gas sector as high gas prices throughout most of 2022 led to an increase in Texas crude production. The demand for housing has slowed due to increasing interest rates and high prices. This has allowed inventories to improve and prices to moderate. Irrigated farmland and ranchland prices have stabilized in the second half of the year while dryland continues to climb. While recession fears loom due to the Federal Reserve's efforts to curb inflation by driving up interest rates, the Texas economy remains strong and well positioned to endure potential setbacks.

Agriculture in Texas suffered throughout much of 2022 due to extreme drought conditions around the state causing crop failures and herd reductions. Multiple Peril Crop Insurance (MPCI) served as a safety net for many due to strong insurance commodity prices. The lack of rainfall early in the spring also meant farmers were spared high input costs. Conditions improved in the fourth quarter, allowing ranchers to begin to rebuild their herds and a good start to winter wheat crops. Capital Farm Credit continues to see strong credit quality throughout the loan portfolio. The following is a review and outlook of some of the key commodities served by the association and a summary of industries and economic factors that impact our part-time farmers. The percentages shown were determined based on the outstanding loan volume tied to the specific type of operation or commodity as of December 31, 2022.

Livestock (50.0 percent of the loan portfolio) – Drought and high input costs led to the largest cow herd liquidation in Texas since 2011. It is expected this will lead to a 4 percent reduction in the nation's cow herd next year, leading to higher cattle prices. This could create a challenge as producers look to rebuild their herds.

Crops (15.2 percent of the loan portfolio) – Crop producers also felt the effects of drought conditions in Texas, leading to crop failures throughout the state. High input costs continue to be a concern, leading some farmers to migrate from cotton to grain crops. MPCI will continue to be an important safety net in the coming year, highlighting the importance of the 2023 Farm Bill.

Hunting and recreation (12.3 percent of the loan portfolio) – Rising interest rates and high acreage prices have slowed this sector of the portfolio in the second half of the year. Prices have begun to moderate as demand has cooled, but the continued increase in interest rates will limit growth in this area.

Dairy (5.3 percent of the loan portfolio) – Dairy producers in Texas saw high milk prices accompanied by high input costs in 2022. The dairy industry in Texas continues to grow as processing capacity increases in the state. While margins are expected to shrink slightly, the outlook for dairy producers continues to appear strong.

Utilities (2.7 percent of the loan portfolio) – This sector of the portfolio has recovered from challenges faced in previous years due to the pandemic and extreme weather conditions. Improved infrastructure in Texas has helped to stabilize the industry.

Timber (2.1 percent of the loan portfolio) – Timber production and prices were strong throughout 2022. Lumber prices were strong in the first half of the year but softened in the second half, with declining housing starts and rising interest rates.

Other (12.4 percent of the loan portfolio) – The Federal Reserve continues to tighten monetary policy to fight inflation by raising short-term interest rates and reducing their balance sheet by allowing Treasuries and mortgage-backed securities to mature. They are committed to returning the Consumer Price Index (CPI) to their preferred level of 2 percent. Because of this, economists are projecting further rate hikes in 2023. This has slowed loan demand in the second half of the year, but the association continues to maintain strong credit quality and is anticipating healthy profitability in the coming year.

**Significant Events:**

**Preferred Stock Issuance**

On January 19, 2021 the association issued $200,000 in noncumulative perpetual preferred stock. The decision to issue preferred stock came in response to the high level of loan growth over the last three years. The issuance carries an annual dividend rate of 5.00 percent paid quarterly. The issuance will be callable March 15, 2026, and quarterly thereafter. If not called, the dividend will reset for the next five years to 4.52 percent over the five-year treasury on the call date. The association made dividend payments on March 15, June 15, September 15, and December 15, 2022, for a total amount of $10,000.

**Rating Agency Actions**

*Fitch Ratings Actions*
On January 11, 2021, Fitch Ratings assigned the association an initial long-term issuer default ratings (IDRs) at "BBB" with a stable outlook. Fitch also assigned a rating of "BB-" for the association's noncumulative perpetual preferred stock. Fitch reaffirmed the association's "BBB" with a stable outlook rating on December 12, 2022.

*S&P Global Rating Actions*
On January 11, 2021, S&P assigned the association an initial long-term issuer default rating at "BBB" with a stable outlook. S&P Global Ratings also assigned a rating of "BB" for the association's noncumulative perpetual preferred stock. S&P reaffirmed the association's "BBB" with a stable outlook rating on December 19, 2022.

**Senior Officer Retirements**

On January 26, 2021, the board announced their decision to name Jeff Norte as the chief executive officer, replacing Mr. Novosad effective June 1, 2021. Mr. Norte has over 30 years of banking experience, with more than 10 years at the association, most recently as chief credit officer.

Effective March 15, 2021, Sally Lawson was named chief financial officer. Mrs. Lawson has more than 30 years of financial and accounting experience, with more than 16 years of experience at the association, most recently as vice president of finance.

**Patronage Refunds by Association**

The board of directors approved a $270,028 patronage distribution for 2022. Of that amount, $127,595 of this distribution will be paid in cash in March 2023, and $142,433 will be distributed in the form of nonqualified allocated equity, which means the owners of these distributions will not pay federal income taxes until the equities are retired. It is the board's intention with these allocations to assign ownership of the earnings of the association, allowing the stockholders to benefit more fully from the earnings of the association and to create a method to make future equity distributions in the form of cash. Though there is not a planned retirement of these allocated equities, the board of directors will make an annual evaluation of the association's capital position and determine if some cash retirements of these equities can be made. In 2021, the board of directors approved a $233,769 patronage distribution, with cash patronage payable of $108,069 and $125,700 in nonqualified allocations. In 2020, the board of directors approved a $215,865 patronage distribution, with cash patronage payable of $98,280 and $117,585 in nonqualified allocations. In March of 2021, the association finalized the computation of these distributions, which resulted in an increase in cash patronage payable of $92 for an actual cash distribution of $98,372, which was paid in March 2021.

In September 2022, the board of directors approved a resolution to retire $59,747 in nonqualified allocated equities, which were paid to the recipients in November 2022. The retirement was a distribution of all remaining earnings allocated in 2013. In September 2021, the board of directors approved a resolution to retire $60,000 in nonqualified allocated equities, which were paid to the recipients in December 2021. The retirement was a distribution of all remaining earnings allocated in 2012 and 24 percent of the earnings allocated in 2013. In September 2020, the board of directors approved a resolution to retire $55,000 in nonqualified allocated equities, which were paid to the recipients in November 2020. The retirement was a distribution of 57 percent of the earnings allocated in 2012.

**Patronage Refund Received from Farm Credit Bank of Texas**

The association received income in the form of a direct loan patronage of $61,171, $49,936 and $38,226 from the Farm Credit Bank of Texas (bank), representing 0.64 percent, 0.63 percent and 0.55 percent of the average daily balance of the association's direct loan with the bank at December 31, 2022, 2021 and 2020, respectively. The association also received $3,800, $2,737 and $3,192 in patronage payments from the bank, based on the association's stock investment in the bank at December 31, 2022, 2021 and 2020, respectively. In addition, as a result of the CPP transaction discussed under the "Loan Portfolio" section below, the association received patronage of $1,550, $1,866 and $2,390 in 2022, 2021 and 2020, respectively. Also, the association received a capital markets patronage of $4,588, $4,646 and $5,132 from the bank in 2022, 2021 and 2020 representing approximately 1.00 percent, 1.00 percent and 1.00 percent, respectively, on the year's average daily balance for loan participations sold to the bank.

**Loan Portfolio:**

The association makes and services loans to farmers, ranchers, rural homeowners and certain farm-related businesses. The association's loan volume consists primarily of long-term real estate mortgage loans, production and intermediate-term loans and farm-related business loans including originated and purchased. These loan products are available to eligible borrowers with competitive variable and fixed interest rates. For all loan products, the association is able to lock an interest rate spread for the pricing term of the loan. When the pricing term expires on a loan, the association is subject to a new cost of funds from the bank. However, the association is then also able to establish a new interest spread on the loan to the customer. Pricing terms range from one month on Farm Credit SOFR indexed and prime-indexed products, CME Term SOFR, and from 60 days to 30 years on fixed-rate products. Loan maturities range from one to five years, with annual operating loans comprising the majority of the production loans and five- to 30-year maturities comprising the majority of the mortgage loans. Loans serviced by the association offer several installment payment cycles, the timing of which usually coincides with the seasonal cash-flow capabilities of the borrower.

At December 31, 2022, the association's loan volume was $11,487,825, an increase of $1,031,314 or 9.9 percent from December 31, 2021. Volume increased in 2022 across the portfolio, with the growth in the real estate mortgage loans of $485,375 or 6.0 percent, production intermediate-term loans of $271,075 or 23.6 percent, farm related business loans of $157,168 or 19.4 percent, communication loans of $64,019 or 51.3 percent, energy loans of $53,649 or 61.3 percent, water and waste disposal loans of $10,948 or 801.5 percent and lease receivable loans of $1,115 or 5.9 percent, slightly offset by decreases in rural residential real estate of $11,961 or 10.2 percent and mission-related investments of $74 or 3.9 percent. At December 31, 2021, loan volume was $10,456,511, which was 20.4 percent higher than the December 31, 2020, loan volume of $8,684,131. The credit quality of the association's portfolio has remained strong and improved slightly from the prior year. Loans classified as acceptable were 98.4 percent of the total portfolio at December 31, 2022, in comparison to 97.9 percent of the total portfolio at December 31, 2021, and 96.8 percent at December 31, 2020. Overall, there has been no significant change in the geographical distribution of the portfolio or the types of loans that comprise the portfolio. The composition of the association's loan portfolio is described more fully in detailed tables in Note 4 to the consolidated financial statements, "Loans and Allowance for Credit Losses."

In September 2018, the association completed a sale of $99,586 in loans to the Farm Credit Bank of Texas as part of its capitalized participation pool (CPP). In accordance with this program, the association capitalizes this loan pool with a 6 percent investment in the bank in exchange for the net earnings this pool generates. The CPP program allows the association to manage its capital by controlling the amount of loan volume on the balance sheet. The program recognized earnings of $1,244, $1,615 and $2,068 in 2022, 2021 and 2020, respectively. The earnings from the program are under the control and discretion of FCBT.

At December 31, 2022, 2021 and 2020, the association held two, two and four transactions respectively, which are reported as loans on the consolidated balance sheet totaling $1,803, $1,877 and $5,758, with remaining commitments of $0, $0 and $0 extended under the Rural America Bond Program approved by the FCA. The program is designed to meet the growing and changing needs of agricultural enterprises, agribusinesses and rural communities by providing investment in rural areas.

**Purchase and Sales of Loans:**

The association has obtained loan guarantees from the Federal Agricultural Mortgage Corporation (Farmer Mac) through an arrangement with the bank in the form of standby commitments to purchase qualifying loans. At December 31, 2022, 2021 and 2020, loans totaling $7,558, $8,017 and $9,906, respectively, were guaranteed by these commitments. Fees paid for these guarantees totaled $28, $35 and $45 in 2022, 2021 and 2020, respectively, and are reflected in "other noninterest expense" in the consolidated statement of income.

The association participates in loans with other lenders and is a net seller. As of December 31, 2022, 2021 and 2020, loan participations purchased by the association totaled $2,079,009, $1,440,066 and $1,166,976, or 18.1 percent, 13.8 percent and 13.4 percent of loans, respectively. Included in these amounts are participations purchased from entities outside the System, totaling $3,422, $3,156 and 16,152, or 0.0 percent, 0.0 percent and 0.2 percent of loans, respectively, and $2,075,587, $1,436,910 and $1,150,824, or 18.1 percent, 13.7 percent and 13.3 percent of loans, respectively, from entities within the System. Of the amounts purchased within the System, $344,123, $271,810 and $534,712 were purchased within the district as of December 31, 2022, 2021 and 2022, respectively. The association has also sold participations to other lenders within the System of $2,244,723, $2,143,298 and $1,643,496 as of December 31, 2022, 2021 and 2020, respectively.

**Investments:**

**<u>Agricultural Mortgage-Backed Securities</u>**

During 2010, the association exchanged loans totaling $27,975 for Farmer Mac guaranteed mortgage-backed securities (AMBS). The loans were previously covered under the Long-Term Standby Commitments to Purchase (LTSCP) Agreement with Farmer Mac. These loans were sold to Farmer Mac and then repurchased in the form of a guaranteed AMBS investment. The primary objective in pursuing the AMBS conversion alternative is to reduce the association's credit exposure to Farmer Mac by putting the association in a position to benefit from the United States Treasury line of credit (under Section 8.13 of the Farm Credit Act), which is only available for the payment of Farmer Mac's guarantee obligations on securities, not for its obligations under the LTSCP program. No gain or loss was recognized in the financial statements as a result of the exchange transaction. These AMBS are included in the association's consolidated balance sheet as held-to-maturity investments at an amortized cost balance of $1,496, $1,952 and $2,582 at December 31, 2022, 2021 and 2020, respectively. The association continues to service the loans included in that transaction.

**<u>Point of Purchase Equipment Financing</u>**

The association partners with other Farm Credit associations to facilitate a point of purchase equipment financing program under the name of AgDirect LLP (AgDirect). The AgDirect program operates through independent equipment dealers to originate and refinance agricultural equipment loans. The association's investment in AgDirect was $16,339, $14,902 and $11,067 at December 31, 2022, 2021 and 2020, respectively. Income from this program was $2,054, $1,790 and $1,490 for the years ended December 31, 2022, 2021 and 2020, respectively, and is included in other income in the accompanying Consolidated Statements of Comprehensive Income.

**<u>Relationships with Unincorporated Business Entities</u>**

The association and the bank made investments in a limited partnership, the Advantage Capital Ag Partners L.P., that will provide junior capital to rural and agriculture businesses in the United States. This partnership is a Rural Business Investment Company (RBIC), and the investment by the association and the bank is allowed under the Mission-Related Investment authorities granted in the Farm Credit Act. The association's investment in RBIC was $13,024, $12,225 and $11,384 at December 31, 2022, 2021 and 2020, respectively. The association recorded (loss)/income from this investment in 2022, 2021 and 2020 of ($78), $1,881 and ($2,367), respectively.

**Risk Exposure:**

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

| | **2022** | | | 2021 | | | 2020 | | |
|---|---|---|---|---|---|---|---|---|---|
| | | **Amount** | **%** | | Amount | % | | Amount | % |
| Loans: | | | | | | | | | |
| Nonaccrual loans | **$** | **56,133** | **81.2%** | $ | 38,111 | 78.5% | $ | 48,138 | 83.4% |
| 90 days past due and still accruing interest | | **1,173** | **1.7%** | | 736 | 1.5% | | 212 | 0.4% |
| Formally restructured loans | | **8,933** | **12.9%** | | 8,804 | 18.1% | | 8,792 | 15.2% |
| Other property owned, net | | **2,924** | **4.2%** | | 927 | 1.9% | | 601 | 1.0% |
| Total | **$** | **69,163** | **100.0%** | $ | 48,578 | 100.0% | $ | 57,743 | 100.0% |

At December 31, 2022, 2021 and 2020, loans that were considered impaired were $66,239, $47,651 and $57,142, representing 0.6 percent, 0.5 percent and 0.7 percent of loan volume, respectively. Impaired loans consist of all high-risk assets except other property owned, net. Nonaccrual loans increased $18,022 during 2022 primarily as a result of one large borrower being downgraded. This decrease was recognized primarily in the farm-related business, production and intermediate-term and real estate mortgage sectors. Formally restructured loans increased $129 during 2022. The increase was in the farm-related business sector offset by decreases in the real estate mortgage, production and intermediate-term, and mission related investments sectors. In addition, the association saw an increase in loans 90 days past due and still accruing interest of $437 during 2022 in the production and intermediate-term and communication sectors. Other property owned increased by $1,997 during 2022. Other property owned consists of four properties.

Management also continues to routinely evaluate and monitor counterparty and collateral risks in an effort to avoid concentrations that could result in excess exposure to a single counterparty or type of collateral. The loan portfolio management practices in place have been designed to ensure loans and industries with actual or potential problems are promptly identified, monitored and addressed in a manner that allows the lending staff to work with problem customers and industries through periods of adversity. To help mitigate and diversify credit risk, the association has employed practices including securitization of loans, obtaining credit guarantees and engaging in loan participations.

Except for the relationship between installment due date and seasonal cash-flow capacities of certain borrowers, the association is not affected by any seasonal characteristics. The factors affecting the operations of the association are the same factors that would affect any agricultural real estate lender.

**Allowance for Credit Losses:**

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

| | **2022** | | 2021 | | 2020 | |
|---|---|---|---|---|---|---|
| Allowance for loan losses | **$** | **21,386** | $ | 22,996 | $ | 31,592 |
| Allowance for loan losses to total loans | | **0.2%** | | 0.2% | | 0.4% |
| Allowance for loan losses to nonaccrual loans | | **38.1%** | | 60.3% | | 65.6% |
| Allowance for loan losses to impaired loans | | **32.3%** | | 48.3% | | 55.3% |
| Net charge-offs (recoveries) to average loans | | **0.0%** | | 0.0% | | 0.0% |

The year-end allowance for credit losses is based upon estimates that consider the general financial strength of the overall economy and the agricultural economy, as well as the association's loan portfolio composition, credit administration and prior loan loss experience. The association calculates its allowance in two parts, specific allowances and a general allowance. The association evaluates all loans classified as impaired for a specific allowance. This specific allowance is generally based upon the value of the collateral securing the loan relative to the loan amount outstanding. Allowance for credit losses of $1,639, $4,977 and $3,165 were specifically related to impaired loans totaling $66,239, $47,651 and $57,141 at December 31, 2022, 2021 and 2020, respectively. These specific allowances represent 2.5 percent, 10.4 percent and 5.5 percent of the impaired loans at December 31, 2022, 2021 and 2020, respectively. The association experienced loan charge-offs of $2,080, $752 and $2,137 in 2022, 2021 and 2020, respectively, representing 4.4 percent, 1.3 percent and 2.8 percent of the previous year-end balance of impaired loans. Charge-offs in 2022 were in the production and intermediate-term sector, the energy sector and the real estate mortgage sector. Most of the loan charge-offs in 2021 were primarily in the production and intermediate portfolio as a result of weak commodity prices. In addition, the association recovered loans previously charged off in the amounts of $1,572, $1,133 and $2,262 in 2022, 2021 and 2020, respectively.

The association monitors its general allowance to recognize the trend in the quality of the portfolio. The association uses industry-based loan pools to calculate its general allowance on the loans that are not analyzed specifically. Risk factors are applied to the loan volume in each industry pool based upon current economic conditions and the credit quality of the loans in that pool. Total allowances on loans not considered impaired were $19,747, $18,019 and $28,427 at December 31, 2022, 2021 and 2020, respectively. The allowance for credit losses at December 31, 2022, is considered adequate by management to recognize any inherent losses in the loan portfolio at such dates.

The association also provides line of credit financing to customers to cover short-term and variable needs. As a result, the association has unfunded commitments for which a separate reserve is maintained. This reserve is reported as a liability on the association's consolidated balance sheet.

**Results of Operations:**

The association's net income for the year ended December 31, 2022, was $286,309 as compared with $261,713 for the year ended December 31, 2021, reflecting an increase of $24,596, or 9.4 percent. The association's net income for the year ended December 31, 2020, was $220,258. Net income increased $41,455, or18.8 percent, in 2021 as compared with 2020.

Net interest income for 2022, 2021 and 2020 was $322,799, $280,400 and $247,641, respectively. This reflects increases of $42,399 or 15.1 percent, for 2022 versus 2021 and $32,759 or 13.2 percent, for 2021 versus 2020. Net interest income is the principal source of earnings for the association and is impacted by loan volume, yields on loans and cost of debt. The effects of changes in average volume and interest rates on net interest income over the past three years are presented in the following tables:

| | **2022** | | 2021 | | 2020 | |
|---|---|---|---|---|---|---|
| | **Average Balance** | **Interest** | Average Balance | Interest | Average Balance | Interest |
| Interest-earning assets | **$ 11,054,195** | **$ 553,108** | $ 9,341,168 | $ 437,239 | $ 8,105,137 | $ 416,431 |
| Interest-bearing liabilities | **9,508,904** | **230,309** | 7,878,400 | 156,839 | 6,920,767 | 168,790 |
| Impact of capital | **$ 1,545,291** | | $ 1,462,768 | | $ 1,184,370 | |
| Net interest income | | **$ 322,799** | | $ 280,400 | | $ 247,641 |

| | **2022** | 2021 | 2020 |
|---|---|---|---|
| | **Average Yield** | Average Yield | Average Yield |
| Yield on interest-earning assets | **5.00%** | 4.68% | 5.14% |
| Cost of interest-bearing liabilities | **2.42%** | 1.99% | 2.44% |
| Net interest spread | **2.58%** | 2.69% | 2.70% |

| | **2022 vs. 2021** | | | 2021 vs. 2020 | | |
|---|---|---|---|---|---|---|
| | **Increase (decrease) due to** | | | Increase (decrease) due to | | |
| | **Volume** | **Rate** | **Total** | Volume | Rate | Total |
| Interest income | **$ 80,184** | **$ 35,685** | **$ 115,869** | $ 63,506 | $ (42,698) | $ 20,808 |
| Interest expense | **32,459** | **41,011** | **73,470** | 23,356 | (35,307) | (11,951) |
| Net interest income | **$ 47,725** | **$ (5,326)** | **$ 42,399** | $ 40,150 | $ (7,391) | $ 32,759 |

Though most of the improvement in net interest income for the past three years is due to the increase in loan volume, the association has also benefited from higher levels of capital. This reduced the amount of debt borrowed in relation to loan volume.

Interest income for 2022 increased by $115,869, or 26.5 percent, compared with 2021, due to an increase in loan volume and an increase in interest rates. Interest expense for 2022 increased by $73,470, or 46.8 percent, compared with 2021 primarily due to increased rates and an increase in the direct note balance. The interest rate spread decreased by 11 basis point to 2.58 percent in 2022 from 2.69 percent in 2021, primarily as a result of an increase in interest rates. The interest rate spread decreased by 1 basis point to 2.69 in 2021 from 2.70 in 2020.

Noninterest income for 2022 increased by $9,128, or 10.7 percent, compared to 2021, primarily as a result of an increase in patronage from the bank, an increase in gain on sale of premises and equipment, and an increase in other noninterest income, offset by decreases in loan fees, a decrease in financially related services and a decrease in gain on other property owned, net. The bank paid 64-basis point cash patronage on the association's average direct note borrowings during 2022 compared to 63-basis points in 2021. The increase in patronage from the bank is also a result of an increase in the direct note balance. Noninterest income for 2021 increased by $13,702, or 19.2 percent, compared with 2020, due to an increase in patronage refund received from the bank, an increase in financially related services, an increase in gain on sale of premises and equipment and a gain on other noninterest income, slightly offset by decreases in loan fees and a decrease on gains on other property owned. The bank paid a 63-basis-point cash patronage on the association's average direct note borrowings in 2021 compared with a 55-basis- point patronage in 2020. Gain on sale of premises and equipment increased by $1,119, or 270.9 percent, as a result of the association selling two buildings during the year. Other noninterest income increased $4,719, or 78.9 percent, as a result of an increase in patronage from other farm credit institutions and income generated by the investment in RBIC.

There was a reversal of provision for credit losses of $1,003 in 2022, compared to a reversal of $9,198 in 2021. The decrease in the reversal was primarily a result of further refinement of loss given defaults during 2021. There was a reversal of provision for credit losses of $9,198 in 2021, compared with a provision of $582 in 2020. The reversal was a result of improved collateral values and improved credit quality during 2021. The association was able to collect on loans classified as nonaccrual in 2021 from the prior year.

Noninterest expenses increased in 2022 by $18,787, or 16.6 percent, compared with 2021. All categories of noninterest expense increased during 2022 offset with a decrease in other expense of $140, or 10.6 percent, compared to 2021. The increase is a result of continued COVID-19 restrictions being completely lifted during the entire 2022 fiscal year, implementation of the association's new lending platform, increased headcount and growth in the loan portfolio. The increase was primarily driven by an increase in salaries and employee benefits of $8,376, or 11.5 percent, as a result of increased headcount, and FCSIC premiums of $6,190 or 52.2 percent, as a result of an increase in premium rates and loan volume, compared to 2021. Noninterest expenses increased $14,736 for 2021, or 15.0 percent, compared with 2020. All noninterest expenses increased in 2021 offset with a slight decrease in business insurance expense of $4. Salaries and employee benefits increased by $5,992, or 9.0 percent, as a result of new employees and salary adjustments made to existing employees. FCSIC premiums have increased as a result of increases in the association's loan volume and the premium assessment rate. The remaining noninterest expenses increased primarily as a result of COVID-19 restrictions being lifted. Noninterest expenses decreased $2,927 for 2020, or 2.9 percent, compared with 2019. Noninterest expenses primarily decreased as a result of COVID-19, with the largest decrease in travel of $1,565 or 36.1 percent in 2020 compared with 2019. Other decreases in public and member relations of $804 or 24.3 percent, training of $406 or 42.9 percent and other expenses of $543 or 30.5 percent, were slightly offset by increases in salaries and employee benefits of $355 or 0.5 percent and FCSIC premiums of $789 or 14.5 percent in 2020.

Authoritative accounting guidance requiring the capitalization and amortization of loan origination fees and costs resulted in the capitalization of $5,934, $22,385 and $15,141 for 2022, 2021 and 2020, respectively, in origination fees. The capitalized costs consisted of salaries and benefits totaling $12,993, $17,856 and $14,774 for 2022, 2021 and 2020, respectively, related to the origination of loans. The capitalized fees, net of the capitalized costs, are amortized over the life of the loans as an adjustment to yield in net interest income. The adjustment to net interest income as a result of this amortization was $606, $1,291 and $1,219 for 2022, 2021 and 2020, respectively.

For the year ended December 31, 2022, the association's return on average assets was 2.5 percent, as compared with 2.7 percent and 2.6 percent for the years ended December 31, 2021 and 2020, respectively. For the year ended December 31, 2022, the association's return on average members' equity was 16.4 percent, as compared with 15.9 percent and 16.7 percent for the years ended December 31, 2021 and 2020, respectively.

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

**Liquidity and Funding Sources:**

The interest rate risk inherent in the association's loan portfolio is substantially mitigated through the funding relationship with the bank. The bank manages interest rate risk through its direct loan pricing and asset/liability management process. All of the association's loans are match-funded with debt with similar terms by the bank.

The primary source of liquidity and funding for the association is a direct loan from the bank. The outstanding balance of $9,840,475, $8,873,812 and $7,374,054 as of December 31, 2022, 2021 and 2020, respectively, is recorded as a liability on the association's balance sheet. The note carried a weighted average interest rate of 3.20 percent, 1.80 percent and 1.98 percent at December 31, 2022, 2021 and 2020, respectively. The indebtedness is collateralized by a pledge of substantially all of the association's assets to the bank and is governed by a financing agreement. This increase in note payable to the bank and related accrued interest payable since December 31, 2021, is due to an increase in the association's loan portfolio. The association's average own funds, which represent the amount of the association's loan portfolio funded by the association's equity were $1,648,158, $1,584,894 and $1,303,861 for the years 2022, 2021 and 2020, respectively. The maximum amount the association may borrow from the bank as of December 31, 2022, was $11,043,084 as defined by the general financing agreement. The indebtedness continues in effect until the expiration date of the general financing agreement, which is September 30, 2023, unless sooner terminated by the bank upon the occurrence of an event of default, or by the association, in the event of a breach of this agreement by the bank, upon giving the bank 30 calendar days' prior written notice, or in all other circumstances, upon giving the bank 120 days' prior written notice. The association anticipates the general financing agreement to be renewed by the bank, without any significant adjustments, prior to its expiration.

The liquidity policy of the association is to manage cash balances to maximize debt reduction and to increase accrual loan volume. This policy will continue to be pursued during 2023. As borrower payments are received, they are applied to the association's note payable to the bank.

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

**Capital Resources:**

The association's capital position remains strong, with total members' equity of $1,728,347, $1,633,305 and $1,351,557 at December 31, 2022, 2021 and 2020, respectively. Under regulations governing minimum permanent capital adequacy and other capitalization issues, the association is required to maintain a minimum adjusted permanent capital of 7.0 percent of risk-adjusted assets as defined by the FCA. The permanent capital ratio measures available at-risk capital relative to risk-adjusted assets and off-balance sheet contingencies. The ratio is an indicator of the institution's financial capacity to absorb potential losses beyond that provided in the allowance for loss accounts. The association's permanent capital ratio at December 31, 2022, 2021 and 2020 was 13.1 percent, 14.3 percent and 14.1 percent, respectively.

Under the regulations, the association is required to maintain minimum Common Equity Tier 1 (CET1), Tier 1 Capital, and Total Capital ratios of 4.5 percent, 6.0 percent and 8.0 percent, along with a capital conservation buffer of 2.5 percent applicable to each ratio, respectively. The CET1 Capital ratio is an indicator of the institution's highest quality of capital and consists of unallocated retained earnings, qualifying common cooperative equities (CCEs) that meet the required holding periods and paid-in capital. The Tier 1 Capital ratio is a measure of the institution's quality of capital and financial strength. The Total Capital ratio is supplementary to the Tier 1 Capital ratio, the components of which include qualifying CCEs subject to certain holding periods, and allowance for credit losses subject to certain limitations. The Tier 1 Leverage ratio is used to measure the amount of leverage an institution has incurred against its capital base, of which at least 1.5 percent must be unallocated retained earnings (URE) and URE equivalents. This is the UREE Leverage ratio. The association's Common Equity Tier 1 ratio in 2022, 2021 and 2020 was 11.5 percent, 12.4 percent and 14.0 percent, respectively, and Tier 1 Capital ratio was 13.1 percent, 14.3 percent and 14.0 percent, respectively. The Total Capital ratio was 13.3 percent, 14.5 percent and 14.4 percent at December 31, 2022, 2021 and 2020, respectively. Under the regulations, the association is required to maintain a minimum Tier 1 Leverage ratio of 4.0 percent, along with a leverage buffer of 1.0 percent, and a minimum unallocated retained earnings equivalent (UREE) leverage ratio of 1.5 percent. The association's Tier 1 Leverage ratio at December 31, 2022, 2021 and 2020 was 13.9 percent, 15.0 percent and 14.7 percent, respectively, and UREE Leverage ratio was 5.4 percent, 7.3 percent and 8.4 percent, respectively.

The association has been able to maintain solid levels of capital and strong capital ratios while declaring patronage refunds in cash to its stockholders in the amounts of $127,595, $108,069 and $98,280 in 2022, 2021 and 2020, respectively. The board of directors also issued $142,433, $125,700 and $117,585 in nonqualified written notices of allocation in 2022, 2021 and 2020, respectively. In addition, the association retired $59,747, $60,000 and $55,000 of previously allocated nonqualified written notices of allocation in September 2022, 2021 and 2020, respectively. See Note 11 to the consolidated financial statements, "Members' Equity," included in this annual report, for further information.

The association utilizes income pools to determine and allocate the patronage refunds for its customers. Each patronage-eligible customer's loan(s) is assigned to a respective pool based upon common characteristics to service and account for such loans. For 2022, 2021 and 2020, the association utilized a participations purchased pool, a participations sold pool and a general loan pool. The participations purchased pool includes all patronage-eligible loans that are purchased from other farm credit entities. The sold loan pool includes any portion of a loan that the association originates but sells to another entity. The general pool includes all other patronage eligible loans not included in the other pools. Net income is calculated for each pool by including all the net interest income and other income from the loans in the pool and a reasonable allocation of association expenses for each pool. The allocation of expenses is based upon the costs to service and account for the loans in the pool. Net income for each pool is determined by subtracting the allocation of expenses from the income of the loans in the pool. Any net income from the pool is eligible for distribution only to the customers with loans in that pool. If a pool does not generate net income, there are no earnings available for distribution to those customers with loans in that pool. All pools generated earnings available for distribution in 2022, 2021 and 2020.

**Regulatory Matters:**

At December 31, 2022, the association was not under written agreements with the Farm Credit Administration.

On January 5, 2021, the FCA posted an informational memorandum providing guidance to the Farm Credit System on managing challenges associated with COVID-19. The informational memorandum provided supplements on flood insurance requirements, consumer financial protection, and electronic delivery of borrower rights notices. On January 12, 2021, the FCA posted a supplement to its January 5, 2021, informational memorandum, which provided updated guidance to Farm Credit System institutions on issues related to COVID-19. The supplement covers regulatory capital requirements for Paycheck Protection Program loans. On January 28, 2021, the FCA posted a supplement to its January 5, 2021, informational memorandum, which provided updated guidance to Farm Credit System institutions on issues related to COVID-19. The supplement discusses matters related to association annual meetings and elections during the 2021 calendar year.

On February 5, 2021, the FCA posted an informational memorandum on maintaining and using stockholder lists. The informational memorandum provides institutions with guidance on maintaining the lists and using them to establish who should receive voting and financial information.

On June 30, 2021, the FCA posted an advance notice of proposed rulemaking to seek public comments on how to amend or restructure bank liquidity regulations. The FCA is considering whether to amend the existing liquidity regulatory framework so banks can better withstand crises that adversely impact liquidity. The comment period ended on November 27, 2021.

On August 26, 2021, the FCA published a proposed rule in the Federal Register on defining and establishing risk-weightings for high-volatility commercial real estate (HVCRE) exposures. The comment period ended on January 24, 2022.

On September 9, 2021, the FCA adopted a final rule on the tier 1/tier 2 capital framework. The rule clarifies the regulations, simplifies certain requirements, and changes the lending and leasing limit base calculation to be computed using total capital instead of permanent capital. It also codifies guidance provided in FCA Bookletter 068. On October 1, 2021, the FCA published the final rule on the tier 1/tier 2 capital framework in the Federal Register. The final rule became effective on January 1, 2022.

On December 8, 2021, the FCA posted an informational memorandum on managing the LIBOR transition. The informational memorandum provides institutions with guidance on the transition away from LIBOR, clarifies the meaning of new LIBOR contracts, and provides guidance on using alternative reference rates.

**Significant Recent Accounting Pronouncements and Critical Accounting Policies:**

Refer to Note 2, "Summary of Significant Accounting Policies," in this annual report for disclosures of recent accounting pronouncements that may impact the association's consolidated financial position and results of operations and for critical accounting policies.

**Relationship with the Bank:**

The association's statutory obligation to borrow only from the bank is discussed in Note 10 to the consolidated financial statements, "Note Payable to the Bank," included in this annual report. The bank's ability to access additional capital from the association is discussed in Note 2 to the consolidated financial statements, "Summary of Significant Accounting Policies," included in this annual report, within the section "Capital Stock Investment in the Bank." The bank's role in mitigating the association's exposure to interest rate risk is described in the section "Liquidity and Funding Sources" of this Management's Discussion and Analysis and in Note 10 to the consolidated financial statements, "Note Payable to the Bank," included in this annual report.

The bank provides computer systems to support the critical operations of all district associations. In addition, the association has operating systems and facility-based systems that are not supported by the bank. As disclosed in Note 14 to the consolidated financial statements, "Related Party Transactions," included in this annual report, the bank provides many services that the association can utilize. Expenses included in purchased services may include purchased services such as administrative services, marketing, information systems, accounting services and allocations of expenses incurred by the bank passed through to the associations.

## Report of Independent Auditors

To the Board of Directors of Capital Farm Credit, ACA

### *Opinion*

We have audited the accompanying consolidated financial statements of Capital Farm Credit, ACA and its subsidiaries (the "Association"), which comprise the consolidated balance sheets as of December 31, 2022, 2021 and 2020, and the related consolidated statements of comprehensive income, changes in members' equity and cash flows for the years then ended, including the related notes (collectively referred to as the "consolidated financial statements").

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Association as of December 31, 2022, 2021 and 2020, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### *Basis for Opinion*

We conducted our audit in accordance with auditing standards generally accepted in the United States of America (US GAAS). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are required to be independent of the Association and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### *Responsibilities of Management 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, and for 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.

In preparing the consolidated financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Association's ability to continue as a going concern for one year after the date the consolidated financial statements are available to be issued.

### *Auditors' Responsibilities for the Audit of the Consolidated Financial Statements*

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with US GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the consolidated financial statements.

In performing an audit in accordance with US GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements.
- Obtain an understanding of internal control relevant to the audit 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, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the consolidated financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Association's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

***Other Information***

Management is responsible for the other information included in the annual report. The other information comprises the information included in the 2022 Annual Report, but does not include the consolidated financial statements and our auditors' report thereon. Our opinion on the consolidated financial statements does not cover the other information, and we do not express an opinion or any form of assurance thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and consider whether a material inconsistency exists between the other information and the consolidated financial statements, or the other information otherwise appears to be materially misstated. If, based on the work performed, we conclude that an uncorrected material misstatement of the other information exists, we are required to describe it in our report.

PricewaterhouseCoopers LLP

Austin, Texas
March 9, 2023

**CAPITAL FARM CREDIT, ACA**
**CONSOLIDATED BALANCE SHEETS**
**(dollars in thousands)**

| | December 31, | | |
|---|---|---|---|
| | **2022** | **2021** | **2020** |
| **ASSETS** | | | |
| Cash | **$ -** | $ - | $ 2 |
| Loans | **11,487,825** | 10,456,511 | 8,684,131 |
| Less: Allowance for losses | **(21,386)** | (22,996) | (31,592) |
| Net Loans | **11,466,439** | 10,433,515 | 8,652,539 |
| Accrued interest receivable - loans | **84,311** | 64,852 | 61,956 |
| Accrued interest receivable - investments | **28** | 24 | 34 |
| Investment -- held-to-maturity | **1,496** | 1,952 | 2,582 |
| Investment in and receivable from the Bank: | | | |
| Capital stock | **191,460** | 159,199 | 142,764 |
| Receivable | **21,295** | 21,842 | 18,615 |
| Investment in Rural Business Investment Company | **13,024** | 12,225 | 11,384 |
| Investments in other Farm Credit Institutions | **16,928** | 15,131 | 11,270 |
| Other property owned, net | **2,924** | 927 | 601 |
| Premises and equipment, net | **17,120** | 13,768 | 14,995 |
| Right of use asset - leases | **8,263** | 8,840 | 10,137 |
| Other assets | **18,942** | 19,592 | 16,761 |
| Total assets | **$ 11,842,230** | $ 10,751,867 | $ 8,943,640 |
| **LIABILITIES** | | | |
| Note payable to the Bank | **$ 9,840,475** | $ 8,873,812 | $ 7,374,054 |
| Advanced conditional payments | **11,034** | 11,686 | 14,564 |
| Accrued interest payable | **25,933** | 14,274 | 13,141 |
| Lease liabilities | **8,492** | 9,051 | 10,320 |
| Drafts outstanding | **378** | 904 | 335 |
| Patronage distributions payable | **127,603** | 108,075 | 98,285 |
| Unfunded post-retirement medical obligation | **21,420** | 27,286 | 27,472 |
| Reserve for unfunded commitments | **456** | 357 | 578 |
| Other liabilities | **78,092** | 73,117 | 53,334 |
| Total liabilities | **10,113,883** | 9,118,562 | 7,592,083 |
| **MEMBERS' EQUITY** | | | |
| Capital stock and participation certificates | **28,337** | 28,410 | 27,043 |
| Preferred Stock | **200,000** | 200,000 | - |
| Nonqualified allocated retained earnings | **885,831** | 803,147 | 737,454 |
| Unallocated retained earnings | **610,986** | 604,705 | 590,617 |
| Accumulated other comprehensive income (loss) | **3,193** | (2,957) | (3,557) |
| Total members' equity | **1,728,347** | 1,633,305 | 1,351,557 |
| Total liabilities and members' equity | **$ 11,842,230** | $ 10,751,867 | $ 8,943,640 |

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

**CAPITAL FARM CREDIT, ACA**
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**
**(dollars in thousands)**

| | Year Ended December 31, | | |
|---|---|---|---|
| | **2022** | **2021** | **2020** |
| **Interest Income** | | | |
| Loans | **$ 553,023** | $ 437,136 | $ 416,279 |
| Investments | **85** | 103 | 152 |
| Total interest income | **553,108** | 437,239 | 416,431 |
| **Interest Expense** | | | |
| Note Payable to the Bank | **230,270** | 156,836 | 168,774 |
| Advance conditional payments | **39** | 3 | 16 |
| Total interest expense | **230,309** | 156,839 | 168,790 |
| Net interest income | **322,799** | 280,400 | 247,641 |
| **Provision for Loan Losses** | | | |
| (Reversal) provision for credit losses | **(1,003)** | (9,198) | 582 |
| Net interest income after provision for losses | **323,802** | 289,598 | 247,059 |
| **Noninterest Income** | | | |
| Patronage income from the Bank | **71,109** | 59,185 | 48,940 |
| Loan fees | **5,934** | 8,862 | 12,165 |
| Financially related services income | **3,552** | 4,716 | 3,755 |
| Gain on sale of premises and equipment, net | **2,015** | 1,532 | 413 |
| Gain on other property owned, net | **-** | 79 | 118 |
| Other noninterest income | **11,591** | 10,699 | 5,980 |
| Total noninterest income | **94,201** | 85,073 | 71,371 |
| **Noninterest Expense** | | | |
| Salaries and employee benefits | **80,906** | 72,530 | 66,538 |
| Insurance Fund premium | **18,050** | 11,860 | 6,214 |
| Occupancy and equipment | **5,989** | 5,898 | 5,355 |
| Advertising | **4,544** | 3,983 | 3,950 |
| Purchased services | **4,243** | 3,809 | 2,591 |
| Public and member relations | **3,463** | 2,623 | 2,505 |
| Travel | **3,310** | 3,152 | 2,765 |
| Supervisory and exam expense | **2,280** | 2,056 | 1,975 |
| Data processing | **1,984** | 1,841 | 1,592 |
| Training | **1,937** | 803 | 541 |
| Business insurance expense | **1,216** | 1,012 | 1,016 |
| Communications | **1,155** | 1,109 | 1,029 |
| Director's expense | **1,095** | 907 | 862 |
| Loss on other property owned, net | **338** | - | - |
| Other noninterest expenses | **1,185** | 1,325 | 1,239 |
| Total noninterest expenses | **131,695** | 112,908 | 98,172 |
| Income before income tax | **286,308** | 261,763 | 220,258 |
| (Benefit from) provision for income tax | **(1)** | 50 | - |
| Net income | **$ 286,309** | $ 261,713 | $ 220,258 |
| Other comprehensive gain (loss): | | | |
| Change in postretirement benefit plans | **6,150** | 600 | (634) |
| Income tax expense related items of other comprehensive income | **-** | - | - |
| Other comprehensive gain (loss), net of tax | **6,150** | 600 | (634) |
| **COMPREHENSIVE INCOME** | **$ 292,459** | $ 262,313 | $ 219,624 |

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

**CAPITAL FARM CREDIT, ACA**

**CONSOLIDATED STATEMENTS OF CHANGES IN MEMBERS' EQUITY**
**(dollars in thousands)**

| | Capital Stock/ Participation Certificates | Preferred Stock | Retained Earnings Non qualified Allocated | Retained Earnings Unallocated | Accumulated Other Comprehensive Loss | Total Members' Equity |
|---|---|---|---|---|---|---|
| Balance at December 31, 2019 | $ 25,980 | $ - | $ 674,877 | $ 586,224 | $ (2,923) | $ 1,284,158 |
| Comprehensive income: | | | | | | |
| Net income | - | - | - | 220,258 | - | 220,258 |
| Other comprehensive gain | - | - | - | - | (634) | (634) |
| Capital stock/participation certificates issued | 5,728 | - | - | - | - | 5,728 |
| Capital stock/participation certificates/ allocated equities retired | (4,665) | - | (55,000) | - | - | (59,665) |
| Patronage distributions declared: | | | | | | |
| Cash | - | - | - | (98,280) | - | (98,280) |
| Other adjustments | - | - | (8) | - | - | (8) |
| Nonqualified allocations | - | - | 117,585 | (117,585) | - | - |
| Balance at December 31, 2020 | 27,043 | - | 737,454 | 590,617 | (3,557) | 1,351,557 |
| Net income | - | - | - | 261,713 | - | 261,713 |
| Other comprehensive (loss) | - | - | - | - | 600 | 600 |
| Capital stock/participation certificates issued | 6,507 | - | - | - | - | 6,507 |
| Capital stock/participation certificates/ allocated equities retired | (5,140) | - | (60,000) | - | - | (65,140) |
| Preferred stock issued | - | 200,000 | - | - | - | 200,000 |
| Issuance cost on preferred stock | - | - | - | (4,707) | - | (4,707) |
| Preferred stock dividends | - | - | - | (9,056) | - | (9,056) |
| Patronage distributions declared: | | | | | | |
| Cash | - | - | - | (108,069) | - | (108,069) |
| Other adjustments | - | - | (7) | (93) | - | (100) |
| Nonqualified allocations | - | - | 125,700 | (125,700) | - | - |
| Balance at December 31, 2021 | 28,410 | 200,000 | 803,147 | 604,705 | (2,957) | 1,633,305 |
| Net income | - | - | - | 286,309 | - | 286,309 |
| Other comprehensive gain | - | - | - | - | 6,150 | 6,150 |
| Capital stock/participation certificates issued | 5,135 | - | - | - | - | 5,135 |
| Capital stock/participation certificates/ allocated equities retired | (5,208) | - | (59,747) | - | - | (64,955) |
| Preferred stock dividends | - | - | - | (10,000) | - | (10,000) |
| Patronage distributions declared: | | | | | | |
| Cash | - | - | - | (127,595) | - | (127,595) |
| Other adjustments | - | - | (2) | - | - | (2) |
| Nonqualifed allocations | - | - | 142,433 | (142,433) | - | - |
| **Balance at December 31, 2022** | **$ 28,337** | **$ 200,000** | **$ 885,831** | **$ 610,986** | **$ 3,193** | **$ 1,728,347** |

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

**CAPITAL FARM CREDIT, ACA**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**
**(dollars in thousands)**

| | Year Ended December 31, | | |
|---|---|---|---|
| | **2022** | 2021 | 2020 |
| **Cash flows from operating activities:** | | | |
| Net income | **$ 286,309** | $ 261,713 | $ 220,258 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| (Reversal of)/provision for loan losses | **(1,003)** | (9,198) | 582 |
| Provision on other property owned | **40** | 12 | 221 |
| Loss/(gain) on other property owned | **272** | (52) | (251) |
| Depreciation and amortization | **5,434** | 5,768 | 2,146 |
| Amortization of Right of Use Asset | **577** | 1,297 | 534 |
| Loss/(gain) on sale of premises and equipment, net | **2,015** | (1,532) | (391) |
| Loss/(gain) on investment in RBIC | **78** | (1,881) | 2,367 |
| (Increase)/decrease in accrued interest receivable | **(19,463)** | (2,886) | 9,439 |
| Decrease/(increase) in other assets | **1,197** | (6,058) | (720) |
| Accretion of the discounted lease liability | **(559)** | (1,269) | (494) |
| Increase/(decrease) in accrued interest payable | **11,659** | 1,133 | (3,016) |
| Increase in other liabilities | **5,259** | 20,197 | 7,553 |
| Net cash provided by operating activities | **$ 291,815** | $ 267,244 | $ 238,228 |
| **Cash flows from investing activities:** | | | |
| (Increase) in loans, net | **$ (1,039,603)** | $ (1,777,114) | $ (863,950) |
| Cash recoveries of loans previously charged off | **1,572** | 1,133 | 2,262 |
| (Proceeds from) investment in AgDirect, LLP | **(1,797)** | (3,861) | (1,412) |
| (Proceeds from) investment in RBIC | **(877)** | 1,040 | (1,120) |
| (Proceeds from) investment in the Bank | **(32,261)** | (16,435) | (7,753) |
| Decrease in investments held to maturity | **456** | 630 | 836 |
| (Purchases of) premises and equipment | **(5,131)** | (2,220) | (4,000) |
| Proceeds from sales of premises and equipment | **(2,048)** | 2,449 | 1,801 |
| Proceeds from sales of other property owned | **278** | 458 | 1,660 |
| Net cash used in investing activities | **$ (1,079,411)** | $ (1,793,920) | $ (871,676) |

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

**CAPITAL FARM CREDIT, ACA**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**
**(dollars in thousands)**

| | Year Ended December 31, | | |
|---|---|---|---|
| | **2022** | 2021 | 2020 |
| **Cash flows from financing activities:** | | | |
| Net increase in note payable to the Bank | **$ 966,663** | $ 1,499,758 | $ 769,656 |
| Increase/(decrease) in drafts outstanding | **(526)** | 569 | (1,775) |
| (Decrease)/increase in advance conditional payments | **(652)** | (2,878) | 8,062 |
| Issuance of capital stock and participation certificates | **5,135** | 6,507 | 5,728 |
| Issuance of preferred stock | **-** | 200,000 | - |
| Issuance cost on preferred stock | **-** | (4,707) | - |
| Retirement of capital stock, participation certificates | **-** | - | - |
| and allocated equities | **(64,955)** | (65,140) | (59,665) |
| Cash dividends paid | **(10,000)** | (9,056) | - |
| Patronage distributions paid | **(108,069)** | (98,379) | (88,558) |
| Net cash provided by financing activities | **$ 787,596** | $ 1,526,674 | $ 633,448 |
| Net (decrease) in cash | **-** | **(2)** | **-** |
| Cash at the beginning of the year | **-** | 2 | 2 |
| Cash at the end of the year | $ - | $ - | $ 2 |
| **Supplemental schedule of noncash investing and financing activities:** | | | |
| Loans transferred to other property owned upon loan foreclosure | **$ 2,587** | $ 744 | $ 1,372 |
| Net loans charged off | **2,080** | 752 | 2,137 |
| Patronage distributions declared | **127,595** | 108,069 | (98,280) |
| **Supplemental cash information:** | | | |
| Cash paid during the year for: | | | |
| Interest | **$ 218,650** | $ 155,706 | $ 171,806 |
| Income taxes | **-** | - | - |

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

**CAPITAL FARM CREDIT, ACA**
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**
**(ALL DOLLAR AMOUNTS IN THOUSANDS)**

## NOTE 1 — ORGANIZATION AND OPERATIONS:

A. Organization: Capital Farm Credit, ACA, including its wholly owned subsidiaries, Capital Farm Credit, PCA and Capital Farm Credit, FLCA (collectively called the association), is a member-owned cooperative that provides credit and credit-related services to, or for the benefit of, eligible borrowers/stockholders for qualified agricultural purposes in 192 counties in the state of Texas.

   The association is a lending institution of the Farm Credit System (System), a nationwide system of cooperatively owned banks and associations that was established by Acts of Congress to meet the credit needs of American agriculture and is subject to the provisions of the Farm Credit Act of 1971, as amended (Act). At December 31, 2022, the System was composed of three Farm Credit Banks (FCBs) and their affiliated associations, one Agricultural Credit Bank (ACB) and its affiliated associations, the Federal Farm Credit Banks Funding Corporation (Funding Corporation) and various service and other organizations.

   The Farm Credit Bank of Texas (bank) and its related associations are collectively referred to as the "district." The bank provides funding to all associations within the district and is responsible for supervising certain activities of the district associations. At December 31, 2022, the district consisted of the bank, one FLCA and 13 ACA parent companies (including Capital Farm Credit, ACA), which have two wholly owned subsidiaries, an FLCA and a PCA, operating in or servicing the states of Alabama, Louisiana, Mississippi, New Mexico and Texas. ACA parent companies provide financing and related services through their FLCA and PCA subsidiaries. The FLCA makes secured long-term agricultural real estate and rural home mortgage loans. The PCA makes short- and intermediate-term loans for agricultural production or operating purposes.

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

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

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

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

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

## NOTE 2 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

**Basis of Presentation and Consolidation**

The consolidated financial statements (the "financial statements") and the accounting and reporting policies of the association have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) and prevailing practices within the banking industry. In consolidation, all significant intercompany accounts and transactions are eliminated and all material wholly owned and majority-owned subsidiaries are consolidated unless GAAP requires otherwise. The consolidated financial statements include the accounts of Capital Farm Credit, PCA and Capital Farm Credit, FLCA.

**Use of Estimates**

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the financial statements. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the valuation of deferred tax assets, the determination of fair value of financial instruments and subsequent impairment analysis. Significant estimates are discussed in these footnotes, as applicable.

**Reclassifications**

Certain amounts in prior years' consolidated financial statements have been reclassified to conform to current financial statement presentation.

A. Recently Issued or Adopted Accounting Pronouncements:

In March 2020, the FASB issued guidance titled "Facilitation of the Effects of Reference Rate Reform on Financial Reporting (Reference Rate Reform)." The guidance provides optional expedients and exceptions for applying GAAP to contracts, hedging relationships and other transactions affected by reference rate reform to ease the potential burden related to reference rate reform (transition away from the London Inter-Bank Offered Rate (LIBOR)). The optional amendments are effective as of March 12, 2020 through December 31, 2022.

In January 2021, the FASB issued an update to Reference Rate Reform whereby certain derivative instruments may be modified to change the rate used for margining, discounting, or contract price alignment. An entity may elect to apply the new amendments on a full retrospective basis as of any date from the beginning of an interim period that includes or is subsequent to March 12, 2020, or on a prospective basis to new modifications from any date within an interim period that includes or is subsequent to the date of the update, up to the date that financial statements are available to be issued. These amendments do not apply to contract modifications made or new hedging relationships entered into after December 31, 2022, and existing hedging relationships evaluated for effectiveness in periods after December 31, 2022.

The association adopted the FASB guidance titled "Measurement of Credit Losses on Financial Instruments" on January 1, 2023. This guidance established a single allowance framework for all financial assets measured at amortized cost and certain off-balance sheet credit exposures. The guidance requires management to consider in its estimate of allowance for credit losses (ACL) relevant historical events, current conditions and reasonable and supportable forecasts that affect the collectability of the assets. Prior to the adoption, the allowance for loan losses represented management's estimate of the probable credit losses inherent in its loan portfolio and certain unfunded commitments. In addition, the guidance amends existing impairment guidance for held-to-maturity and available-for-sale investments to incorporate an allowance, which will allow for the reversal of credit impairments in the event that the credit of an issuer improves. The adoption of this guidance resulted in a net increase in the association's allowance for credit losses of approximately $2,684 million and a corresponding decrease in retained earnings.

In March 2022, the Financial Accounting Standards Board (FASB) issued an update titled "Financial Instruments - Credit Losses: Troubled Debt Restructurings and Vintage Disclosures." The guidance eliminates the accounting guidance for troubled debt restructurings (TDRs) by creditors while enhancing disclosure requirements for certain loan refinancings and restructurings when a borrower is experiencing financial difficulty. The creditor will have to apply the guidance to determine whether a modification results in a new loan or a continuation of an existing loan. In addition to the TDR guidance, the update requires public business entities to disclose current period gross write-offs by year of origination for financing receivables and net investments in leases within the scope of the credit losses standard. These amendments were effective for the association upon adoption of the measurement of credit losses on financial instruments standard on January 1, 2023.

B. Cash: Cash, as included in the balance sheet and statement of cash flows, represents cash on hand and on deposit at banks.

C. Investments: The association's investments include mortgage-backed securities issued by the Federal Agricultural Mortgage Corporation (Farmer Mac) for which the association has the intent and ability to hold to maturity and that are consequently classified as held-to-maturity. Held-to-maturity investments are carried at cost, adjusted for the amortization of premiums and accretion of discounts. Changes in the fair value of these investments are not recorded unless the investment is deemed to be other-than-temporarily impaired. Impairment is considered to be other-than-temporary if the present value of cash flows expected to be collected from the debt security is less than the amortized cost basis of the security (any such shortfall is referred to as a "credit loss"). If 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 should be recognized currently in earnings in an amount equal to the entire difference between fair value and amortized cost. If a credit loss exists, but 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 should be separated into (i) the estimated amount relating to credit loss and (ii) the amount relating to all other factors. Only the estimated credit loss amount is recognized currently in earnings, with the remainder of the loss amount recognized in other comprehensive income.

   The association holds additional investments in accordance with mission-related investment and other investment programs approved by the FCA. These programs allow the association to make investments that further the System's mission to serve rural America. Mission-related investments for which the association has the intent and ability to hold to maturity are classified as held-to-maturity and carried at cost, adjusted for the amortization of premiums and accretion of discounts.

   In accordance with the Farm Credit Administration regulations, the association, with the approval of its bank, may purchase and hold investments to manage risks. The association must identify and evaluate how the investments that it purchases contributes to management of its risks. Only securities that are issued by, or are unconditionally guaranteed or insured as to the timely payment of principal and interest by, the United States government or its agencies are investments that the association may acquire. The total amount of investments allowed must not exceed 10 percent of the association's total outstanding loans.

   The association may also hold additional investments in accordance with other investment programs approved by the Farm Credit Administration. These programs allow the association to make investments that further the System's mission to serve rural America. These other investments are not included in the investment limitation specified by the Farm Credit Administration regulations. Mortgage-backed securities issued by Farmer Mac are considered other investments. Other investments for which the association has the intent and ability to hold to maturity are classified as held-to-maturity and carried at cost, adjusted for the amortization of premiums and accretion of discounts.

D. Loans and Allowance for Credit Losses: Long-term real estate mortgage loans generally have original maturities ranging from five to 40 years. Substantially all short- and intermediate-term loans for agricultural production or operating purposes have maturities of 10 years or less. Loans are carried at their principal amount outstanding adjusted for charge-offs and deferred loan fees or costs. Interest on loans is accrued and credited to interest income based upon the daily principal amount outstanding.

   Authoritative accounting guidance requires loan origination fees and direct loan origination costs to be capitalized and the net fee or cost to be amortized over the life of the related loan as an adjustment to yield.

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

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

A restructured loan constitutes a troubled debt restructuring (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. A concession is generally granted in order to minimize the association's economic loss and avoid foreclosure. Concessions vary by program and are borrower-specific and may include interest rate reductions, term extensions, payment deferrals or the acceptance of additional collateral in lieu of payments. In limited circumstances, principal may be forgiven. A loan restructured in a troubled debt restructuring is an impaired loan.

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

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

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

The credit risk-rating methodology is a key component of the association's allowance for credit losses evaluation and is incorporated into its loan underwriting standards and internal lending limit. The allowance for credit losses is maintained at a level considered adequate by management to provide for probable losses inherent in the loan portfolio. The year-end allowance for credit losses is based upon estimates that consider the general financial strength of the overall economy and the agricultural economy specifically, loan portfolio composition, credit administration and the portfolio's prior loan loss experience. The association calculates its allowance in two parts, specific allowances and general allowance. The association evaluates all loans classified as impaired for a specific allowance. Generally, for loans individually evaluated the allowance for credit losses represents the difference between the loan balance and the present value of the cash flows expected to be collected discounted at the loan's effective interest rate, or at the fair value of the collateral, less estimated costs to sell, if the loan is collateral-dependent. For those loans collectively evaluated for impairment, the allowance for credit losses is determined using factors related to its risk rating and its repayment source.

The association also provides line of credit financing to customers to cover short-term and variable needs. As a result, the association has unfunded commitments for which a separate reserve is maintained. This reserve is reported as a liability on the association's consolidated balance sheet. The combined amounts of the allowance for loan losses and the reserve for unfunded commitments are referred to as the "allowance for credit losses."

Transfers of an entire financial asset, group of entire financial assets or a participating interest in an entire financial asset are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the association; (2) the transferee obtains the right to pledge or exchange the transferred assets; and (3) the association does not maintain effective control over the transferred assets.

The association purchases loan and lease participations from other System and non-System entities to generate additional earnings and diversify risk related to existing commodities financed and the geographic area served. Additionally, the association sells a portion of certain large loans to other System and non-System entities to reduce risk and comply with established lending limits. Loans are sold and the sale terms comply with requirements under Accounting Standards Codification (ASC) 860 "Transfers and Servicing."

E. Capital Stock Investment in the Bank: The association's investment in the bank is in the form of Class A voting capital stock and allocated retained earnings. This investment is adjusted annually. The bank requires a minimum stock investment of 2 percent of the association's average borrowing from the bank. This investment is carried at cost plus allocated equities from the bank in the accompanying consolidated balance sheet.

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

F. Other Property Owned, Net: Other property owned, net, consists of real and personal property acquired through foreclosure or deed in lieu of foreclosure and is recorded at fair value less estimated selling costs upon acquisition. Any initial reduction in the carrying amount of a loan to the fair value of the collateral received is charged to the allowance for credit losses. On at least an annual basis, 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 and expenses from operations and carrying value adjustments are included in net gains (losses) on other property owned in the statements of comprehensive income.

G. Premises and Equipment: Premises and equipment are carried at cost less accumulated depreciation. Land is carried at cost and not depreciated. Depreciation is provided on the straight-line method using estimated useful lives of each asset. Estimate useful lives are as follows: Buildings are 40 years, leasehold improvements are 15 years, furniture and equipment are 10 years, computer equipment and software are three years and automobiles are five years. Gains and losses on dispositions are reflected in current operations. Maintenance and repairs are charged to operating expense, and improvements are capitalized. Long-lived assets are reviewed for impairment whenever events or circumstances indicate the carrying amount of an asset group may not be recoverable.

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

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

   The structure of the district's DB plan is characterized as multiemployer, since neither the assets, liabilities nor costs of the plan are segregated or separately accounted for by the associations. No portion of any surplus assets is available to the associations, nor are the associations required to pay for plan liabilities upon withdrawal from the plans. As a result, the associations recognize as pension cost the required contribution to the plans for the year. Contributions due and unpaid are recognized as a liability. For the DB plan, the association recognized costs of $3,083, $4,435 and $1,834 for the years ended December 31, 2022, 2021 and 2020, respectively.

   Participants in the DC plan generally include employees who elected to transfer from the DB plan prior to January 1, 1996, and employees hired on or after January 1, 1996. Participants in the DC plan direct the placement of their employers' contributions, 5.0 percent of eligible pay for the year ended December 31, 2022, made on their behalf into various investment alternatives. The association recognized costs for the DC plan of $3,284, $2,813 and $2,662 for the years ended December 31, 2022, 2021 and 2020, respectively.

   The association also participates in the Farm Credit Benefits Alliance 401(k) plan, which requires the associations to match 100 percent of employee contributions up to 3.0 percent of eligible earnings and to match 50 percent of employee contributions for the next 2.0 percent of employee contributions, up to a maximum employer contribution of 4.0 percent of eligible earnings. Association 401(k) plan costs are expensed as incurred. The association's contributions to the 401(k) plan were $2,399, $2,218 and $2,090 for the years ended December 31, 2022, 2021 and 2020, respectively.

In addition to the DB plan, the DC plan and the Farm Credit Benefits Alliance 401(k) plan discussed above, the association also sponsors a defined contribution nonqualified supplemental 401(k) plan. The purpose of the plan is (a) to provide eligible employees (those with compensation in excess of $100 in the immediately preceding tax year) of the association who participate in the 401(k) plan with benefits in excess of the limitations on benefits imposed; (b) to allow a means for those employees to make pretax deferrals of additional amounts payable to them to a future payment date; and (c) to allow a means for participating employers to provide discretionary deferred income to those employees. The associated liabilities are included in the association's consolidated balance sheet in other liabilities. The total expenses of the nonqualified plan included in the association's employee benefit costs were $144, $617 and $864 for the years ended December 31, 2022, 2021 and 2020, respectively.

In addition to pension benefits, the association provides certain health care and life insurance benefits to qualifying retired employees (other postretirement benefits). These benefits are not characterized as multiemployer and, consequently, the liability for these benefits is included in other liabilities on the consolidated balance sheets. Association employees hired after January 1, 2004, will be eligible for retiree medical benefits for themselves and their spouses but will be responsible for 100 percent of the related premiums.

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

Deferred income taxes have not been provided by the association on patronage stock distributions from the bank prior to January 1, 1993, the adoption date of FASB guidance on "Accounting for Income Taxes." Management's intent is (1) to permanently invest these and other undistributed earnings in the bank, thereby indefinitely postponing their conversion to cash or (2) to pass through any distribution related to pre-1993 earnings to association borrowers through qualified patronage allocations.

The association has not provided deferred income taxes on amounts allocated to the association that relate to the bank's post-1992 earnings to the extent that such earnings will be passed through to association borrowers through qualified patronage allocations. Additionally, deferred income taxes have not been provided on the bank's post-1992 unallocated earnings. The bank currently has no plans to distribute unallocated bank earnings and does not contemplate circumstances that, if distributions were made, would result in taxes being paid at the association level.

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

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

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

Level 2 — Observable inputs other than quoted prices included within Level 1 that are observable for the asset or liability either directly or indirectly. Level 2 inputs include the following: (a) quoted prices for similar assets or liabilities in active markets; (b) quoted prices for identical or similar assets or liabilities in markets that are not active so that they are traded less frequently than exchange-traded instruments, the prices are not current or principal market information is not released publicly; (c) inputs other than quoted prices that are observable such as interest rates and yield curves, prepayment speeds, credit risks and default rates; and (d) inputs derived principally from or corroborated by observable market data by correlation or other means. This category generally includes certain U.S. government and agency mortgage-backed debt securities, corporate debt securities and derivative contracts. Pension plan assets that are derived from observable inputs, including corporate bonds and mortgage-backed securities, are reported in Level 2. The association does not have any assets that fall within this level.

Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities are considered Level 3. These unobservable inputs reflect the reporting entity's own assumptions about assumptions that market participants would use in pricing the asset or liability. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. This category generally includes certain private equity investments, retained residual interests in securitizations, asset-backed securities, highly structured or long-term derivative contracts, and certain loans and other property owned. Pension plan assets such as certain mortgage-backed securities that are supported by little or no market data in determining the fair value are included in Level 3.

The fair value disclosures are disclosed in Note 15, "Fair Value Measurements."

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

**NOTE 3 — INVESTMENTS:**

**Investments Held-to-Maturity**

The association's held-to-maturity investments consists of Farmer Mac guaranteed agricultural mortgage-backed securities (AMBS). A summary of the amortized cost and fair value of investment securities held-to-maturity is as follows:

| **December 31, 2022** | **Amortized Cost** | **Gross Unrealized Gains** | **Gross Unrealized Losses** | **Fair Value** | **Weighted Average Yield** | **Weighted Average Life (Years)** |
|---|---|---|---|---|---|---|
| Agricultural mortgage-backed securities | **$ 1,496** | $ - | **$ (69)** | **$ 1,427** | **5.22%** | **8.34** |

| December 31, 2021 | **Amortized Cost** | **Gross Unrealized Gains** | **Gross Unrealized Losses** | **Fair Value** | **Weighted Average Yield** | **Weighted Average Life (Years)** |
|---|---|---|---|---|---|---|
| Agricultural mortgage-backed securities | $ 1,952 | $ 49 | $ - | $ 2,001 | 4.47% | 2.69 |

| December 31, 2020 | **Amortized Cost** | **Gross Unrealized Gains** | **Gross Unrealized Losses** | **Fair Value** | **Weighted Average Yield** | **Weighted Average Life (Years)** |
|---|---|---|---|---|---|---|
| Agricultural mortgage-backed securities | $ 2,582 | $ 66 | $ - | $ 2,648 | 4.70% | 3.15 |

The Farmer Mac AMBS were received in exchange for mortgage loans that were previously covered under the long-term standby commitments to purchase agreement with Farmer Mac. No gain or loss was recognized in the financial statements upon completion of the exchange transactions. Terms of the agreement call for a guarantee fee of 20-50 basis points to be paid to Farmer Mac and for the association to receive a 30-basis-point fee for servicing the underlying loans.

## NOTE 4 — LOANS AND ALLOWANCE FOR CREDIT LOSSES:

A summary of loans as of December 31 follows:

| | **2022** | | 2021 | | 2020 | |
|---|---|---|---|---|---|---|
| Loan Type | **Amount** | **%** | Amount | % | Amount | % |
| Production agriculture: | | | | | | |
| Real estate mortgage | **$ 8,629,085** | **75.1%** | $ 8,143,710 | 77.9% | $ 6,739,225 | 77.5% |
| Production and intermediate- term | **1,420,590** | **12.4%** | 1,149,515 | 11.0% | 954,191 | 11.0% |
| Farm-related business | **969,269** | **8.4%** | 812,101 | 7.8% | 705,645 | 8.1% |
| Communication | **188,748** | **1.7%** | 124,729 | 1.2% | 99,968 | 1.2% |
| Energy | **141,142** | **1.2%** | 87,493 | 0.8% | 52,007 | 0.6% |
| Rural residential real estate | **104,966** | **0.9%** | 116,927 | 1.1% | 110,330 | 1.3% |
| Lease receivables | **19,908** | **0.2%** | 18,793 | 0.2% | 15,241 | 0.2% |
| Water and waste disposal | **12,314** | **0.1%** | 1,366 | 0.0% | 1,483 | 0.0% |
| Mission-related investments | **1,803** | **0.0%** | 1,877 | 0.0% | 6,041 | 0.1% |
| Total | **$ 11,487,825** | **100.0%** | $ 10,456,511 | 100.0% | $ 8,684,131 | 100.0% |

At December 31, 2022, the association held two transactions, which are reported as loans on the consolidated balance sheet totaling $1,803 and with $0 in remaining commitments extended under the Rural America Bond Program approved by the FCA. The program is designed to meet the growing and changing needs of agricultural enterprises, agribusinesses and rural communities by providing qualified loans in rural areas.

The association has purchased and sold participation interests with other parties in order to diversify risk, manage loan volume and comply with Farm Credit Administration regulations. The following table presents information regarding participations purchased and sold as of December 31, 2022:

| | Other Farm Credit Institutions | | Non-Farm Credit Institutions | | Total | |
|---|---|---|---|---|---|---|
| | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold |
| Real estate mortgage | $ 281,734 | $ 1,048,640 | $ - | $ - | $ 281,734 | $ 1,048,640 |
| Production and intermediate-term | $ 689,683 | $ 1,075,849 | $ 1,291 | $ - | $ 690,974 | $ 1,075,849 |
| Farm-related business | $ 740,255 | $ 120,234 | $ 2,131 | $ - | $ 742,386 | $ 120,234 |
| Communication | $ 188,748 | $ - | $ - | $ - | $ 188,748 | $ - |
| Energy | $ 141,142 | $ - | $ - | $ - | $ 141,142 | $ - |
| Lease receivables | $ 19,908 | $ - | $ - | $ - | $ 19,908 | $ - |
| Water and waste disposal | $ 12,314 | $ - | $ - | $ - | $ 12,314 | $ - |
| Mission-related investments | $ 1,803 | $ - | $ - | $ - | $ 1,803 | $ - |
| Total | $ 2,075,587 | $ 2,244,723 | $ 3,422 | $ - | $ 2,079,009 | $ 2,244,723 |

Loan Volume by Office

| **Offices** | **2022** | 2021 | 2020 |
|---|---|---|---|
| Capital Markets* | **18.7%** | 15.1% | 14.2% |
| Bryan | **3.4%** | 3.6% | 3.9% |
| Burnet | **3.0%** | 2.8% | 2.5% |
| Austin | **2.6%** | 2.7% | 2.8% |
| Kerrville | **2.6%** | 2.6% | 3.0% |
| San Antonio | **2.6%** | 2.5% | 2.9% |
| Lubbock | **2.6%** | 2.7% | 3.2% |
| Hondo | **2.5%** | 2.8% | 2.5% |
| Fredericksburg | **2.5%** | 2.7% | 2.5% |
| Katy | **2.3%** | 2.3% | 2.1% |
| Rosenberg | **2.3%** | 2.2% | 2.2% |
| Dalhart | **2.3%** | 2.2% | 1.9% |
| Conroe | **2.2%** | 2.4% | 3.1% |
| Uvalde | **2.0%** | 2.1% | 2.0% |
| Mason | **2.0%** | 2.1% | 2.2% |
| New Braunfels | **2.0%** | 2.0% | 1.8% |
| Bowie | **1.9%** | 1.9% | 1.4% |
| El Campo | **1.9%** | 2.2% | 1.7% |
| La Grange | **1.8%** | 1.9% | 2.2% |
| San Angelo | **1.6%** | 1.7% | 1.8% |
| Dayton | **1.5%** | 1.7% | 2.0% |
| Temple | **1.5%** | 1.6% | 1.9% |
| Robstown | **1.5%** | 1.7% | 1.7% |
| Bellville | **1.5%** | 1.6% | 1.7% |
| Clifton | **1.4%** | 1.5% | 0.8% |
| Muleshoe | **1.4%** | 2.3% | 3.3% |
| Lockhart | **1.4%** | 1.4% | 1.3% |
| Jourdanton | **1.4%** | 1.5% | 1.5% |
| Waco | **1.3%** | 1.4% | 1.5% |
| San Saba | **1.3%** | 1.4% | 1.4% |
| Kenedy | **1.2%** | 1.3% | 1.3% |
| Edna | **1.2%** | 1.4% | 1.8% |
| Taylor | **1.1%** | 1.2% | 1.4% |
| Seminole | **1.1%** | 1.1% | 0.0% |
| Madisonville | **1.0%** | 1.1% | 1.1% |
| Laredo | **1.0%** | 1.0% | 1.1% |
| Lamesa | **1.0%** | 1.3% | 1.2% |
| Round Rock | **0.9%** | 1.0% | 0.3% |
| Edinburg | **0.9%** | 0.9% | 1.1% |
| Bay City | **0.9%** | 0.9% | 1.0% |
| Hereford | **0.8%** | 0.9% | 1.9% |
| Wichita Falls | **0.8%** | 1.0% | 1.2% |
| Pampa | **0.8%** | 0.9% | 0.9% |
| Abilene | **0.8%** | 0.9% | 0.8% |
| Dimmitt | **0.8%** | 0.8% | 0.0% |
| Spur | **0.8%** | 0.8% | 0.6% |
| Stamford | **0.7%** | 0.8% | 1.0% |
| Perryton | **0.7%** | 0.6% | 0.8% |
| Munday | **0.7%** | 0.7% | 0.8% |
| All Other Offices | **5.8%** | 4.8% | 4.7% |
| Total | **100.0%** | 100.0% | 100.0% |

*Capital Markets loans include loans purchased from other entities and/or outside of the association’s territory.

Snyder and Crockett were moved to “All Other Offices” in 2021. El Paso and Alpine offices were moved to “All Other Offices” in 2020 for prior year presentations.

The association's concentration of credit risk in various agricultural commodities is shown in the following table. Though the amounts represent the association's maximum potential credit risk as it relates to recorded loan principal, a substantial portion of the association's lending activities is collateralized, and the association's exposure to credit loss associated with lending activities is reduced accordingly. An estimate of the association's credit risk exposure is considered in the determination of the allowance for credit losses.

| | **2022** | | 2021 | | 2020 | |
|---|---|---|---|---|---|---|
| Operation/Commodity | **Amount** | **%** | Amount | % | Amount | % |
| Livestock | **$ 5,738,490** | **50.0%** | $ 5,330,858 | 51.0% | $ 4,306,945 | 49.6% |
| Crops | **1,749,333** | **15.2%** | $ 1,700,133 | 16.2% | $ 1,595,403 | 18.3% |
| Hunting | **1,412,061** | **12.3%** | $ 1,291,789 | 12.4% | $ 970,580 | 11.2% |
| Dairy | **602,687** | **5.3%** | $ 517,939 | 5.0% | $ 433,783 | 5.0% |
| Utilities | **308,188** | **2.7%** | $ 219,586 | 2.1% | $ 156,197 | 1.8% |
| Timber | **243,112** | **2.1%** | $ 250,397 | 2.4% | $ 308,932 | 3.6% |
| Rural home loans | **187,114** | **1.6%** | $ 200,001 | 1.9% | $ 200,044 | 2.3% |
| Poultry | **108,117** | **0.9%** | $ 87,465 | 0.8% | $ 93,836 | 1.1% |
| Industrial/organic chemical | **7,928** | **0.1%** | $ 8,573 | 0.1% | $ 9,950 | 0.1% |
| Other | **1,130,795** | **9.8%** | $ 849,770 | 8.1% | $ 608,461 | 7.0% |
| Total | **$ 11,487,825** | **100.0%** | $ 10,456,511 | 100.0% | $ 8,684,131 | 100.0% |

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

To mitigate the risk of loan losses, the association has obtained loan guarantees in the form of standby commitments to purchase qualifying loans from Farmer Mac through an arrangement with the bank. The agreements, which will remain in place until the loans are paid in full, give the association the right to sell the loans identified in the agreements to Farmer Mac in the event of defaults (typically four months past due), subject to certain conditions. At December 31, 2022, 2021 and 2020, loans totaling $7,558, $8,017 and $9,906, respectively, were guaranteed by these commitments. Fees paid for these guarantees totaled $28, $35 and $45 in 2022, 2021 and 2020, respectively, and are reflected in "other noninterest expense" in the consolidated statements of comprehensive income.

Nonperforming loans are loans for which it is probable that all principal and interest will not be collected according to the contractual terms. Nonperforming assets (including related accrued interest) and related credit quality statistics are as follows:

| | **December 31, 2022** | December 31, 2021 | December 31, 2020 |
|---|---|---|---|
| **Nonaccrual loans:** | | | |
| Real estate mortgage | **$ 25,539** | $ 16,450 | $ 26,919 |
| Farm-related business | **16,401** | 2,005 | 2,555 |
| Production and intermediate-term | **9,950** | 8,662 | 16,472 |
| Energy | **2,818** | 10,742 | 1,936 |
| Lease receivables | **1,297** | - | - |
| Residential real estate | **128** | 252 | 256 |
| Total nonaccrual loans | **$ 56,133** | $ 38,111 | $ 48,138 |
| **Accruing restructured loans:** | | | |
| Real estate mortgage | **$ 4,432** | $ 5,147 | $ 4,960 |
| Production and intermediate-term | **1,091** | 1,936 | 2,060 |
| Farm-related business | **1,741** | - | - |
| Mission related investments | **1,822** | 1,896 | 1,972 |
| Total accruing restructured loans | **$ 9,086** | $ 8,979 | $ 8,992 |
| **Accruing loans 90 days or more past due:** | | | |
| Production and intermediate-term | **1,186** | 785 | 212 |
| Total accruing loans 90 days or more past due | **$ 1,186** | $ 785 | $ 212 |
| Total nonperforming loans | **$ 66,405** | $ 47,875 | $ 57,342 |
| Other property owned, net | **2,924** | 927 | 601 |
| Total nonperforming assets | **$ 69,329** | $ 48,802 | $ 57,943 |

One credit quality indicator utilized by the bank and the association is the Farm Credit Administration Uniform Loan Classification System that categorizes loans into five categories. The categories are defined as follows:

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

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

| | **2022** | 2021 | 2020 |
|---|---|---|---|
| **Real estate mortgage** | | | |
| Acceptable | **98.9%** | 98.6% | 97.6% |
| OAEM | **0.6%** | 0.9% | 1.3% |
| Substandard/doubtful | **0.5%** | 0.5% | 1.1% |
| | **100.0%** | 100.0% | 100.0% |
| **Production and intermediate-term** | | | |
| Acceptable | **98.1%** | 96.8% | 92.1% |
| OAEM | **0.8%** | 1.1% | 4.1% |
| Substandard/doubtful | **1.1%** | 2.1% | 3.8% |
| | **100.0%** | 100.0% | 100.0% |
| **Farm-related business** | | | |
| Acceptable | **94.0%** | 94.1% | 94.3% |
| OAEM | **1.6%** | 4.7% | 4.2% |
| Substandard/doubtful | **4.4%** | 1.2% | 1.5% |
| | **100.0%** | 100.0% | 100.0% |
| **Rural residential real estate** | | | |
| Acceptable | **98.4%** | 98.8% | 98.6% |
| OAEM | **1.4%** | 0.8% | 1.0% |
| Substandard/doubtful | **0.2%** | 0.4% | 0.4% |
| | **100.0%** | 100.0% | 100.0% |
| **Communication** | | | |
| Acceptable | **100.0%** | 100.0% | 100.0% |
| OAEM | **-** | - | - |
| Substandard/doubtful | **-** | - | - |
| | **100.0%** | 100.0% | 100.0% |
| **Energy** | | | |
| Acceptable | **98.0%** | 87.8% | 94.3% |
| OAEM | **-** | - | - |
| Substandard/doubtful | **2.0%** | 12.2% | 5.7% |
| | **100.0%** | 100.0% | 100.0% |
| **Mission-related investments** | | | |
| Acceptable | **100.0%** | 100.0% | 100.0% |
| OAEM | **-** | - | - |
| Substandard/doubtful | **-** | - | - |
| | **100.0%** | 100.0% | 100.0% |
| **Lease receivables** | | | |
| Acceptable | **74.2%** | 94.1% | 91.9% |
| OAEM | **19.3%** | - | - |
| Substandard/doubtful | **6.5%** | 5.9% | 8.1% |
| | **100.0%** | 100.0% | 100.0% |
| **Water and waste disposal** | | | |
| Acceptable | **100.0%** | 100.0% | 100.0% |
| OAEM | **-** | - | - |
| Substandard/doubtful | **-** | - | - |
| | **100.0%** | 100.0% | 100.0% |
| **Total loans** | | | |
| Acceptable | **98.4%** | 97.9% | 96.8% |
| OAEM | **0.7%** | 1.2% | 1.8% |
| Substandard/doubtful | **0.9%** | 0.9% | 1.4% |
| | **100.0%** | 100.0% | 100.0% |

There were no loans and related interest in the loss category.

The following table provides an aging analysis of past due loans (including accrued interest) as of December 31:

| **December 31, 2022** | 30-89 Days Past Due | 90 Days or More Past Due | Total Past Due | Not Past Due or less than 30 Days Past Due | Total Loans | Loans >90 Days and Accruing |
|---|---|---|---|---|---|---|
| Real estate mortgage | **$ 70,127** | **$ 16,698** | **$ 86,825** | **$ 8,608,541** | **$ 8,695,366** | **-** |
| Production and intermediate-term | **35,003** | **7,738** | **42,741** | **1,389,733** | **1,432,474** | **1,186** |
| Farm-related business | **9,083** | **-** | **9,083** | **964,982** | **974,065** | **-** |
| Rural residential real estate | **1,536** | **43** | **1,579** | **103,752** | **105,331** | **-** |
| Communication | **-** | **-** | **-** | **188,994** | **188,994** | **-** |
| Energy | **-** | **-** | **-** | **141,783** | **141,783** | **-** |
| Mission-related investments | **-** | **-** | **-** | **1,822** | **1,822** | **-** |
| Lease receivables | **-** | **1,297** | **1,297** | **18,686** | **19,983** | **-** |
| Water and waste disposal | **-** | **-** | **-** | **12,318** | **12,318** | **-** |
| Total | **$ 115,749** | **$ 25,776** | **$ 141,525** | **$ 11,430,611** | **$ 11,572,136** | **$ 1,186** |

| December 31, 2021 | 30-89 Days Past Due | 90 Days or More Past Due | Total Past Due | Not Past Due or less than 30 Days Past Due | Total Loans | Loans >90 Days and Accruing |
|---|---|---|---|---|---|---|
| Real estate mortgage | $ 66,499 | $ 5,969 | $ 72,468 | $ 8,126,322 | $ 8,198,790 | $ - |
| Production and intermediate-term | 6,774 | 4,910 | 11,684 | 1,144,529 | 1,156,213 | 785 |
| Farm-related business | 408 | - | 408 | 813,956 | 814,364 | - |
| Rural residential real estate | 1,775 | - | 1,775 | 115,533 | 117,308 | - |
| Communication | - | - | - | 124,841 | 124,841 | - |
| Energy | - | 8,076 | 8,076 | 79,660 | 87,736 | - |
| Mission-related investments | - | - | - | 1,896 | 1,896 | - |
| Lease receivables | - | - | - | 18,849 | 18,849 | - |
| Water and waste disposal | - | - | - | 1,366 | 1,366 | - |
| Total | $ 75,456 | $ 18,955 | $ 94,411 | $ 10,426,952 | $ 10,521,363 | $ 785 |

| December 31, 2020 | 30-89 Days Past Due | 90 Days or More Past Due | Total Past Due | Not Past Due or less than 30 Days Past Due | Total Loans | Loans >90 Days and Accruing |
|---|---|---|---|---|---|---|
| Real estate mortgage | $ 51,809 | $ 9,724 | $ 61,533 | $ 6,730,330 | $ 6,791,863 | $ - |
| Production and intermediate-term | 20,624 | 1,276 | 21,900 | 939,039 | 960,939 | 212 |
| Farm-related business | 367 | 307 | 674 | 706,882 | 707,556 | - |
| Rural residential real estate | 1,090 | - | 1,090 | 109,603 | 110,693 | - |
| Communication | - | - | - | 99,998 | 99,998 | - |
| Energy | 1,924 | - | 1,924 | 50,202 | 52,126 | - |
| Mission-related investments | - | - | - | 6,093 | 6,093 | - |
| Lease receivables | - | - | - | 15,333 | 15,333 | - |
| Water and waste disposal | - | - | - | 1,486 | 1,486 | - |
| Total | $ 75,814 | $ 11,307 | $ 87,121 | $ 8,658,966 | $ 8,746,087 | $ 212 |

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

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

As of December 31, 2022, total troubled debt restructured loans was $16,071, including $7,138 classified as nonaccrual and $8,933 classified as accrual, with specific allowance for credit losses of $620. As of December 31, 2022, 2021 and 2020, commitments to lend funds to borrowers whose loan terms have been modified in a troubled debt restructuring were $5,215, $783and $110, respectively. In 2020,the association applied CARES guidance for COVID modifications, and as such, no modifications made under the association's COVID deferral programs met the criteria for TDR as of December 31, 2020.

The following table presents additional information regarding troubled debt restructurings, which includes both accrual and nonaccrual loans with troubled debt restructuring designation that occurred during the year ended December 31, 2022, 2021 and 2020.

The pre-modification outstanding recorded investment represents the recorded investment of the loans as of the quarter end prior to the restructuring. The post-modification outstanding recorded investment represents the recorded investment of the loans as of the quarter end the restructuring occurred.

| **2022** | Balance Pre-TDR designation | | Balance Post-TDR designation | |
|---|---|---|---|---|
| Troubled debt restructurings: | | | | |
| Real estate mortgage | **$** | **1,431** | **$** | **1,434** |
| Production and intermediate- term | | **608** | | **363** |
| Energy | | **8,076** | | **2,150** |
| Total | **$** | **10,115** | **$** | **3,947** |

| 2021 | Balance Pre-TDR designation | | Balance Post-TDR designation | |
|---|---|---|---|---|
| Troubled debt restructurings: | | | | |
| Real estate mortgage | $ | 3,515 | $ | 3,566 |
| Production and intermediate- term | | 432 | | 361 |
| Total | $ | 3,947 | $ | 3,927 |

| 2020 | Balance Pre-TDR designation | | Balance Post-TDR designation | |
|---|---|---|---|---|
| Troubled debt restructurings: | | | | |
| Real estate mortgage | $ | 6,355 | $ | 4,835 |
| Production and intermediate- term | | 2,561 | | 2,489 |
| Total | $ | 8,916 | $ | 7,324 |

In restructurings where principal is forgiven, the amount of the forgiveness is immediately charged off. In restructurings where accrued interest is forgiven, the interest is reversed (if current year interest) or charged off (if prior year interest). There were no charge-offs recorded at the modification date for the year ending December 31, 2022.

The predominant form of concession granted for troubled debt restructuring is an extension of term. Other types of modifications include principal or accrued interest reductions, interest rate decreases and delayed payments, among others. At times, these terms might be offset with incremental payments, collateral or new borrower guarantees, in which case the association assesses all the modified terms to determine if the overall modification qualifies as a troubled debt restructuring.

The following table presents information regarding loans that met the accounting criteria as a troubled debt restructuring and that occurred within the previous 12 months of that year and for which there was a payment default during the period. A payment default is defined as a payment that is 30 days past due after the date the loan was restructured.

| Troubled debt restructurings that subsequently defaulted: | Recorded Investment at December 31, 2022 | | Recorded Investment at December 31, 2021 | | Recorded Investment at December 31, 2020 | |
|---|---|---|---|---|---|---|
| Real estate mortgage | **$** | **-** | $ | 2,365 | $ | - |
| Production and intermediate-term | | **-** | | 198 | | - |
| Total | **$** | **-** | $ | 2,563 | $ | - |

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

| | Loans Modified as TDRs | | |
|---|---|---|---|
| | **December 31, 2022** | December 31, 2021 | December 31, 2020 |
| Troubled debt restructurings: | | | |
| Real estate mortgage | **6,394** | 7,662 | 9,181 |
| Production and intermediate-term | **$ 3,995** | $ 7,752 | $ 9,160 |
| Energy | **2,150** | 1,799 | 1,936 |
| Mission-related investments | **1,803** | 1,877 | 1,972 |
| Farm-related business | **1,729** | - | - |
| Total | **$ 16,071** | $ 19,090 | $ 22,249 |

| | TDRs in Nonaccrual Status* | | |
|---|---|---|---|
| | **December 31, 2022** | December 31, 2021 | December 31, 2020 |
| Troubled debt restructurings: | | | |
| Production and intermediate-term | **$ 2,938** | $ 5,882 | $ 7,100 |
| Real estate mortgage | **2,050** | 2,605 | 4,221 |
| Energy | **2,150** | 1,799 | 1,936 |
| Total | **$ 7,138** | $ 10,286 | $ 13,257 |

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

Additional impaired loan information is as follows:

| | Loan Balance at 12/31/2022 | Unpaid Principal Balance | Related Specific Allowance | Average Impaired Loans | Interest Income Recognized |
|---|---|---|---|---|---|
| **Impaired loans with a related allowance for loan losses:** | | | | | |
| Real estate mortgage | $ 9,946 | $ 10,090 | $ 242 | $ 3,413 | $ 119 |
| Production and intermediate-term | 7,298 | 7,680 | 516 | 3,942 | 140 |
| Farm-related business | - | - | - | 954 | - |
| Rural residential real estate | 24 | 43 | 1 | 27 | - |
| Energy | 2,818 | 3,453 | 583 | 8,511 | - |
| Lease receivables | 977 | 977 | 297 | 163 | 30 |
| Mission-related investments | - | - | - | 53 | - |
| Total | $ 21,063 | $ 22,243 | $ 1,639 | $ 17,063 | $ 289 |
| **Impaired loans with no related specific allowance for loan losses:** | | | | | |
| Real estate mortgage | $ 19,936 | $ 20,043 | $ - | $ 25,573 | $ 261 |
| Production and intermediate-term | 4,881 | 11,282 | - | 9,352 | 283 |
| Farm-related business | 18,131 | 19,149 | - | 4,184 | 621 |
| Rural residential real estate | 104 | 104 | - | 156 | 4 |
| Energy | - | 83 | - | - | - |
| Lease receivables | 321 | 321 | | 756 | 4 |
| Mission-related investments | 1,803 | 1,803 | - | 1,635 | 70 |
| Total | $ 45,176 | $ 52,785 | $ - | $ 41,656 | $ 1,243 |
| **Total impaired loans:** | | | | | |
| Real estate mortgage | $ 29,882 | $ 30,133 | $ 242 | $ 28,986 | $ 380 |
| Production and intermediate-term | 12,179 | 18,962 | 516 | 13,294 | 423 |
| Farm-related business | 18,131 | 19,149 | - | 5,138 | 621 |
| Rural residential real estate | 128 | 147 | 1 | 183 | 4 |
| Energy | 2,818 | 3,536 | 583 | 8,511 | - |
| Lease receivables | 1,298 | 1,298 | 297 | 919 | 34 |
| Mission-related investments | 1,803 | 1,803 | - | 1,688 | 70 |
| Total | $ 66,239 | $ 75,028 | $ 1,639 | $ 58,719 | $ 1,532 |

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

| | Loan Balance at 12/31/2021 | Unpaid Principal Balance | Related Specific Allowance | Average Impaired Loans | Interest Income Recognized |
|---|---|---|---|---|---|
| **Impaired loans with a related allowance for loan losses:** | | | | | |
| Real estate mortgage | $ 566 | $ 564 | $ 70 | $ 261 | $ 18 |
| Production and intermediate-term | 4,286 | 5,301 | 1,133 | 5,602 | 45 |
| Farm-related business | 2,005 | 2,005 | 368 | 2,137 | - |
| Rural residential real estate | 28 | 48 | 2 | 31 | - |
| Energy | 10,742 | 10,749 | 3,357 | 8,145 | 87 |
| Mission-related investments | 127 | 127 | 47 | 431 | 10 |
| Total | $ 17,754 | $ 18,794 | $ 4,977 | $ 16,607 | $ 160 |
| **Impaired loans with no related specific allowance for loan losses:** | | | | | |
| Real estate mortgage | $ 20,941 | $ 20,934 | $ - | $ 31,699 | $ 878 |
| Production and intermediate-term | 6,982 | 13,101 | - | 12,268 | 238 |
| Farm-related business | - | 1,611 | - | 129 | - |
| Rural residential real estate | 224 | 250 | - | 192 | 21 |
| Energy | - | - | - | 7 | - |
| Mission-related investments | 1,750 | 1,750 | - | 1,472 | 108 |
| Total | $ 29,897 | $ 37,646 | $ - | $ 45,767 | $ 1,245 |
| **Total impaired loans:** | | | | | |
| Real estate mortgage | $ 21,507 | $ 21,498 | $ 70 | $ 31,960 | $ 896 |
| Production and intermediate-term | 11,268 | 18,402 | 1,133 | 17,870 | 283 |
| Farm-related business | 2,005 | 3,616 | 368 | 2,266 | - |
| Rural residential real estate | 252 | 298 | 2 | 223 | 21 |
| Energy | 10,742 | 10,749 | 3,357 | 8,152 | 87 |
| Mission-related investments | 1,877 | 1,877 | 47 | 1,903 | 118 |
| Total | $ 47,651 | $ 56,440 | $ 4,977 | $ 62,374 | $ 1,405 |

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

| | Loan Balance at 12/31/2020 | Unpaid Principal Balance | Related Specific Allowance | Average Impaired Loans | Interest Income Recognized |
|---|---|---|---|---|---|
| **Impaired loans with a related allowance for loan losses:** | | | | | |
| Real estate mortgage | $ 121 | $ 121 | $ 4 | $ 122 | $ - |
| Production and intermediate-term | 6,430 | 7,767 | 1,426 | 7,717 | 56 |
| Farm-related business | 2,247 | 2,247 | 368 | 1,807 | - |
| Rural residential real estate | 32 | 55 | 7 | 29 | - |
| Energy | 1,924 | 1,924 | 1,316 | 1,778 | - |
| Mission-related investments | 1,946 | 1,946 | 44 | 1,655 | 122 |
| Total | $ 12,700 | $ 14,060 | $ 3,165 | $ 13,108 | $ 178 |
| **Impaired loans with no related specific allowance for loan losses:** | | | | | |
| Real estate mortgage | $ 31,682 | $ 32,594 | $ - | $ 40,264 | $ 1,398 |
| Production and intermediate-term | 12,210 | 19,549 | - | 17,272 | 394 |
| Farm-related business | 307 | 2,383 | - | 2,824 | 2 |
| Rural residential real estate | 224 | 298 | - | 246 | 16 |
| Energy | 12 | 12 | - | 491 | - |
| Mission-related investments | 6 | 6 | - | 321 | 1 |
| Total | $ 44,441 | $ 54,842 | $ - | $ 61,418 | $ 1,811 |
| **Total impaired loans:** | | | | | |
| Real estate mortgage | $ 31,803 | $ 32,715 | $ 4 | $ 40,386 | $ 1,398 |
| Production and intermediate-term | 18,640 | 27,316 | 1,426 | 24,989 | 450 |
| Farm-related business | 2,554 | 4,630 | 368 | 4,631 | 2 |
| Rural residential real estate | 256 | 353 | 7 | 275 | 16 |
| Energy | 1,936 | 1,936 | 1,316 | 2,269 | - |
| Mission-related investments | 1,952 | 1,952 | 44 | 1,976 | 123 |
| Total | $ 57,141 | $ 68,902 | $ 3,165 | $ 74,526 | $ 1,989 |

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

The association has remaining commitments to lend additional funds to borrowers whose loans were classified as impaired at December 31, 2022, 2021 and 2020, respectively. These commitments totaled $8,581, $833 and $3,947 at December 31, 2022, 2021 and 2020, respectively. The remaining commitments have been considered when establishing the allowance for loan losses, which is recorded in the liabilities section of the consolidated balance sheet as a reserve for unfunded commitments.

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

| | **2022** | 2021 | 2020 |
|---|---|---|---|
| Total interest income that would have been recognized under the original terms | **$ 6,884** | $ 3,822 | $ 4,101 |
| Less: interest income recognized | **1,532** | 1,405 | 1,989 |
| Interest income not recognized | **$ 5,352** | $ 2,417 | $ 2,112 |

A summary of the changes in the allowance for credit losses, unfunded commitments and the ending balance including accrued interest of loans outstanding are as follows:

| | Real Estate Mortgage | Production and Intermediate Term | Farm-related business | Rural Residential Real Estate | Communication | Energy and Water and Waste Disposal | Mission-Related Investments | Lease Receivable | Total |
|---|---|---|---|---|---|---|---|---|---|
| **Allowance for credit losses:** | | | | | | | | | |
| Balance at December 31, 2021 | $ 11,221 | $ 5,501 | $ 2,519 | $ 38 | $ 128 | $ 3,476 | $ 47 | $ 66 | $ 22,996 |
| Charge-offs | (213) | (1,155) | - | - | - | (712) | - | - | (2,080) |
| Recoveries | 142 | 778 | 649 | 3 | - | - | - | - | 1,572 |
| (Reversal) provision for credit losses | 1,906 | (536) | (684) | (3) | 58 | (2,031) | (47) | 334 | (1,003) |
| Transfer from reserve on unfunded commitments | 11 | (76) | (40) | - | 4 | 2 | - | - | (99) |
| Balance at December 31, 2022 | $ 13,067 | $ 4,512 | $ 2,444 | $ 38 | $ 190 | $ 735 | $ - | $ 400 | $ 21,386 |
| **Allowance for credit losses:** individually evaluated for impairment | $ 242 | $ 516 | $ - | $ 1 | $ - | $ 583 | $ - | $ 297 | $ 1,639 |
| **Allowance for credit losses:** collectively evaluated for impairment | $ 12,825 | $ 3,996 | $ 2,444 | $ 37 | $ 190 | $ 152 | $ - | $ 103 | $ 19,747 |
| **Loans, including accrued interest:** | | | | | | | | | |
| Ending Balance at December 31, 2022 | $ 8,695,366 | $ 1,432,474 | $ 974,065 | $ 105,331 | $ 188,994 | $ 154,101 | $ 1,822 | $ 19,983 | $ 11,572,136 |
| Ending balance for loans individually evaluated for impairment | $ 29,970 | $ 12,226 | $ 18,143 | $ 128 | $ - | $ 2,818 | $ 1,822 | $ 1,297 | $ 66,404 |
| Ending balance for loans collectively evaluated for impairment | $ 8,665,396 | $ 1,420,248 | $ 955,922 | $ 105,203 | $ 188,994 | $ 151,283 | $ - | $ 18,686 | $ 11,505,732 |

| | Real Estate Mortgage | Production and Intermediate Term | Farm-related business | Rural Residential Real Estate | Communication | Energy and Water and Waste Disposal | Mission-Related Investments | Lease Receivable | Total |
|---|---|---|---|---|---|---|---|---|---|
| **Allowance for credit losses:** | | | | | | | | | |
| Balance at December 31, 2020 | $ 14,487 | $ 11,394 | $ 3,556 | $ 87 | $ 151 | $ 1,522 | $ 45 | $ 350 | $ 31,592 |
| Charge-offs | - | (752) | - | - | - | - | - | - | (752) |
| Recoveries | 136 | 595 | 395 | 7 | - | - | - | - | 1,133 |
| Provision for credit losses | (3,410) | (5,973) | (1,420) | (56) | (17) | 1,960 | 2 | (284) | (9,198) |
| Transfer to reserve on unfunded commitments | 8 | 237 | (12) | - | (6) | (6) | - | - | 221 |
| Balance at December 31, 2021 | $ 11,221 | $ 5,501 | $ 2,519 | $ 38 | $ 128 | $ 3,476 | $ 47 | $ 66 | $ 22,996 |
| **Allowance for credit losses:** individually evaluated for impairment | $ 70 | $ 1,133 | $ 368 | $ 2 | $ - | $ 3,357 | $ 47 | $ - | $ 4,977 |
| **Allowance for credit losses:** collectively evaluated for impairment | $ 11,151 | $ 4,368 | $ 2,151 | $ 36 | $ 128 | $ 119 | $ - | $ 66 | $ 18,019 |
| **Loans, including accrued interest:** | | | | | | | | | |
| Ending Balance at December 31, 2021 | $ 8,198,790 | $ 1,156,213 | $ 814,364 | $ 117,308 | $ 124,841 | $ 89,102 | $ 1,896 | $ 18,849 | $ 10,521,363 |
| Ending balance for loans individually evaluated for impairment | $ 21,598 | $ 11,383 | $ 2,005 | $ 252 | $ - | $ 10,742 | $ 1,896 | $ - | $ 47,876 |
| Ending balance for loans collectively evaluated for impairment | $ 8,177,192 | $ 1,144,830 | $ 812,359 | $ 117,056 | $ 124,841 | $ 78,360 | $ - | $ 18,849 | $ 10,473,487 |

| | Real Estate Mortgage | Production and Intermediate Term | Farm-related business | Rural Residential Real Estate | Communication | Energy and Water and Waste Disposal | Mission-Related Investments | Lease Receivable | Total |
|---|---|---|---|---|---|---|---|---|---|
| **Allowance for credit losses:** | | | | | | | | | |
| Balance at December 31, 2019 | $ 13,664 | $ 12,989 | $ 3,314 | $ 109 | $ 77 | $ 519 | $ 42 | $ 84 | $ 30,798 |
| Charge-offs | (72) | (1,660) | - | (25) | - | (380) | - | - | (2,137) |
| Recoveries | 510 | 1,538 | 191 | 23 | - | - | - | - | 2,262 |
| Provision for credit losses | 398 | (1,550) | 30 | (20) | 74 | 1,381 | 3 | 266 | 582 |
| Transfer to reserve on unfunded commitments | (13) | 77 | 21 | - | - | 2 | - | - | 87 |
| Balance at December 31, 2020 | $ 14,487 | $ 11,394 | $ 3,556 | $ 87 | $ 151 | $ 1,522 | $ 45 | $ 350 | $ 31,592 |
| **Allowance for credit losses:** individually evaluated for impairment | $ 4 | $ 1,426 | $ 368 | $ 7 | $ - | $ 1,316 | $ 44 | $ - | $ 3,165 |
| **Allowance for credit losses:** collectively evaluated for impairment | $ 14,483 | $ 9,968 | $ 3,188 | $ 80 | $ 151 | $ 206 | $ 1 | $ 350 | $ 28,427 |
| **Loans, including accrued interest:** | | | | | | | | | |
| Ending Balance at December 31, 2020 | $ 6,791,863 | $ 960,939 | $ 707,556 | $ 110,693 | $ 99,998 | $ 53,612 | $ 6,093 | $ 15,333 | $ 8,746,087 |
| Ending balance for loans individually evaluated for impairment | $ 31,605 | $ 18,744 | $ 2,555 | $ 256 | $ - | $ 1,936 | $ 1,972 | $ - | $ 57,068 |
| Ending balance for loans collectively evaluated for impairment | $ 6,760,258 | $ 942,195 | $ 705,001 | $ 110,437 | $ 99,998 | $ 51,676 | $ 4,121 | $ 15,333 | $ 8,689,019 |

## NOTE 5 — LEASES

The association evaluates arrangements at inception to determine if it meets the criteria for a lease. Leases with an initial term of 12 months or less are not recorded on the balance sheet with lease expense recognized on a straight-line basis over the lease term. Operating leases with terms greater than 12 months are included in right of use asset-leases (ROU) and lease liabilities on the balance sheet.

ROU assets represent the association's right to use an underlying asset for the lease term, and lease liabilities represent the association's obligation to make lease payments arising from the lease. Operating ROU assets and liabilities are recognized based on the present value of the lease payments over the lease term. As the rate implicit in the lease is generally not readily determinable for our operating leases, the discount rates used to determine the present value of our lease liability are based on our incremental borrowing rate at the lease commencement date and commensurate with the remaining lease term. Our incremental borrowing rate for a lease is our cost of funds from the bank over a similar term at an amount equal to the lease payments in a similar economic environment. The association's lease terms may include options to extend or terminate the lease when it is reasonably certain that the association will exercise that option. Lease expense for lease payments is recognized on a straight-line basis over the lease term.

The components of lease expense were as follows:

| | | For the year ended December 31, | |
|---|---|---|---|
| | Classification | **2022** | 2021 |
| Operating lease cost | Operating | **$ 2,790** | **$ 2,595** |
| Short-term lease cost | Operating | **205** | **255** |
| Net lease cost | | **$ 2,995** | $ 2,850 |

Other information related to leases was as follows:

| | For the year ended December 31, | |
|---|---|---|
| | **2022** | 2021 |
| Cash paid for amounts included in the measurement of lease liabilities: | | |
| Operating cash flows for operating leases | **$ 2,770** | $ 2,595 |
| Right-of-use assets obtained in exchange for new lease obligations: | | |
| Operating leases | **$ 1,876** | $ 1,032 |

Lease term and discount rate are as follows:

| | **December 31, 2022** | December 31, 2021 |
|---|---|---|
| Weighted average remaining lease term in years: | | |
| Operating leases | **3.00** | 3.43 |
| Weighted average discount rate: | | |
| Operating leases | **2.5%** | 2.1% |

Future minimum lease payments under non-cancellable leases as of December 30, 2022, were as follows:

| | Total Operating Leases |
|---|---|
| 2023 | $ 2,714 |
| 2024 | 2,190 |
| 2025 | 1,383 |
| 2026 | 793 |
| 2027 | 716 |
| Thereafter | 1,036 |
| Total lease payments | 8,832 |
| Less: interest | - |
| Total | $ 8,832 |

The association leases office space in Abilene, Amarillo, Austin, Bay City, Boerne, Brenham, Bryan, Burnet, Conroe, Crockett, Devine, Edinburg, El Paso, Fredericksburg, Harlingen, Hondo, Katy, La Grange, Laredo, Livingston, New Braunfels, Robstown, Round Rock, San Angelo, San Antonio, Victoria, Seminole, Waco and Winnie, Texas. The association also has leases for billboards and postage meters as of December 31, 2022, 2021 and 2020. Lease expense was $2,995, $2,850 and $2,600 for 2022, 2021 and 2020, respectively.

**NOTE 6 – INVESTMENT IN THE FARM CREDIT BANK OF TEXAS:**

The investment in the Farm Credit Bank of Texas is a requirement of borrowing from the bank and is carried at cost plus allocated equities, not fair value, in the accompanying consolidated balance sheet. Estimating the fair value of the association's investment in the Farm Credit Bank of Texas is not practicable because the stock is not traded. The association owns 40.7 percent, 38.8 percent and 39.7 percent of the issued stock of the bank as of December 31, 2022, 2021 and 2020. As of those dates, the bank's assets totaled $35,990,140, $33,093,388 and $28,227,505, respectively, and members' equity totaled $1,623,363, $1,998,196 and $1,991,533, respectively. The bank's earnings were $269,886, $254,591 and $251,137 during 2022, 2021 and 2020, respectively.

**NOTE 7 — PREMISES AND EQUIPMENT:**

Premises and equipment consisted of the following at December 31:

| | **2022** | 2021 | 2020 |
|---|---|---|---|
| Land and Improvements | **$ 5,243** | $ 4,010 | $ 4,056 |
| Building and leasehold improvements | **16,392** | 16,610 | 17,003 |
| Furniture and equipment | **2,030** | 2,021 | 2,276 |
| Computer equipment and software | **3,277** | 2,724 | 2,895 |
| Automobiles | **8,019** | 7,571 | 7,356 |
| Construction in progress | **49** | 3 | 345 |
| | **35,010** | 32,939 | 33,931 |
| Accumulated depreciation | **(17,890)** | (19,171) | (18,936) |
| Total | **$ 17,120** | $ 13,768 | $ 14,995 |

**NOTE 8 – OTHER PROPERTY OWNED, NET:**

Net (loss) gain on other property owned, net consisted of the following for the years ended December 31:

| | **2022** | 2021 | 2020 |
|---|---|---|---|
| (Loss) gain on sale of other property | **$ (272)** | $ 52 | $ 251 |
| Carrying value adjustments | **(40)** | (12) | (221) |
| Operating (expense) income, net | **(26)** | 39 | 88 |
| Net (loss) gain on other property owned | **$ (338)** | $ 79 | $ 118 |

The association's other property owned (OPO) at December 31, 2022, includes four properties totaling 8,140 acres. All these properties have been individually appraised, and the carrying amounts are not in excess of appraised values at December 31, 2022.

**NOTE 9 – OTHER ASSETS AND OTHER LIABILITIES:**

Other assets comprised the following at December 31:

| | **2022** | 2021 | 2020 |
|---|---|---|---|
| Nonqualified deferred compensation trust | **8,339** | 11,121 | 9,365 |
| Prepaid captive insurance premium | **$ 3,047** | $ 2,565 | $ 2,771 |
| Crop insurance commission receivable | **2,360** | 2,988 | 2,091 |
| Acquisition intangibles | **1,345** | 1,606 | 1,888 |
| Other assets | **3,851** | 1,312 | 646 |
| Total assets | **$ 18,942** | $ 19,592 | $ 16,761 |

Other liabilities comprised the following at December 31:

| | | **2022** | | 2021 | | 2020 |
|---|---|---|---|---|---|---|
| Accounts payable | **$** | **28,397** | $ | 27,547 | $ | 24,671 |
| FCS insurance payable | | **18,050** | | 11,860 | | 6,214 |
| Nonqualified deferred compensation payable | | **8,339** | | 11,121 | | 9,365 |
| Annual leave payable | | **4,089** | | 3,501 | | 3,097 |
| Other liabilities | | **19,217** | | 19,088 | | 9,987 |
| Total liabilities | **$** | **78,092** | $ | 73,117 | $ | 53,334 |

**NOTE 10 — NOTE PAYABLE TO THE BANK:**

The interest rate risk inherent in the association's loan portfolio is substantially mitigated through the funding relationship with the bank. The bank manages interest rate risk through its direct loan pricing and asset/liability management process. The association's indebtedness to the bank represents borrowings by the association to fund the majority of its loan portfolio. The indebtedness is collateralized by a pledge of substantially all of the association's assets and is governed by a general financing agreement. The interest rate on the direct loan is based upon the bank's cost of funding the loans the association has outstanding to its borrowers. The indebtedness continues in effect until the expiration date of the general financing agreement, which is September 30, 2023, unless sooner terminated by the bank upon the occurrence of an event of default, or by the association, in the event of a breach of this agreement by the bank, upon giving the bank 30 calendar days prior written notice, or in all other circumstances, upon giving the bank 120 days prior written notice.

The total amount and the weighted average interest rate of the association's direct loan from the bank at December 31, 2022, 2021 and 2020 were $9,840,475 at 3.20 percent, $8,873,812 at 1.80 percent and $7,374,054 at 1.98 percent, respectively.

Under the Act, the association is obligated to borrow only from the bank unless the bank approves borrowing from other funding sources. The bank and FCA regulations have established limitations on the association's ability to borrow funds based on specified factors or formulas relating primarily to credit quality and financial condition. At December 31, 2022, 2021 and 2020, the association's note payable was within the specified limitations. The maximum amount the association may borrow from the bank as of December 31, 2022, was $11,043,084 as defined by the general financing agreement. This borrowing limit changes as the borrowing base increases or decreases.

In addition to borrowing limits, the financing agreement establishes certain covenants including limits on leases, investments, other debt and dividend and patronage distributions; minimum standards for return on assets and for liquidity; and maintaining records, reporting financial information and establishing policies and procedures. Remedies specified in the general financing agreement associated with the covenants include additional reporting requirements, development of action plans, increases in interest rates on indebtedness and reduction of lending limits or repayment of indebtedness. As of and for the years ended December 31, 2022, 2021 and 2020, the association was not subject to remedies associated with the covenants in the general financing agreement.

**NOTE 11 — MEMBERS' EQUITY:**

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

**Preferred Stock**

On January 19, 2021, the association issued $200,000 in noncumulative perpetual preferred stock. The decision to issue preferred stock came in response to the high level of loan growth over the last three years. The issuance carries an annual dividend rate of 5.00 percent paid quarterly. The issuance will be callable March 15, 2026, and quarterly thereafter. If not called, the dividend will reset for the next five years to 4.52 percent over the five-year treasury on the call date. The association made dividend payments on March 15, June 15, September 15, and December 15, 2022, for a total amount of $10,000.

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

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

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

Each owner of Class B capital stock is entitled to a single vote, though participation certificates provide no voting rights to their owners except in a case where a new issuance of preferred stock has been submitted to stockholders affected by the preference.

Within two years of repayment of a loan, the association capital bylaws require the conversion of any borrower's outstanding Class B and participation certificates to Class A stock. Class A stock has no voting rights except in a case where a new issuance of preferred stock has been submitted to stockholders affected by the preference. Redemption of capital stock and participation certificates is made solely at the discretion of the association's board of directors. At December 31, 2022, 2021 and 2020, the association did not have any material Class A stock outstanding.

During 2020, the stockholders approved revision of the capitalization bylaws to allow for the issuance of noncumulative perpetual preferred stock. All stock and allocated equities are at-risk. Net losses recorded by the association shall first be applied against unallocated retained earnings. To the extent such losses exceed unallocated retained earnings, such losses would be applied in accordance with association bylaws and be borne first on a pro-rata basis by holders of all allocated equities and then on a pro rata basis by all holders of Class A stock, Class B capital stock and participation certificates and then on a pro-rata basis by all holders of preferred stock. In the event of liquidation or dissolution of the association, any assets of the association remaining after payment or retirement of all liabilities shall first be distributed to the holders of preferred stock pro-rata in proportion to the number of shares of preferred stock then outstanding until an amount equal to the aggregate par value of all shares of such preferred stock issued and outstanding has been distributed to such holders; second to the holders of stock and participation certificates pro rata in proportion to the number of shares or units of stock or participation certificates then outstanding until an amount equal to the aggregate par value or unit value of all shares of such stock and participation certificates issued and outstanding has been distributed to such holders; third, to the holders of qualified allocated earnings on the basis of the oldest allocations first, until an amount equal to the balance outstanding in this account has been distributed to the holders; fourth, to the holders of nonqualified allocated earnings on a pro rata basis until an amount equal to the total of all notices outstanding has been distributed to the holders; and fifth, any remaining assets of the association in excess of the association's obligations to external parties and to the bank shall be distributed to the members, in proportion to which the aggregate patronage of each such member bears to the total patronage of all such parties insofar as practicable, unless provided by law.

Patronage distributions may be paid as the board of directors may determine by resolution subject to capitalization requirements as defined by the FCA. Amounts not distributed are retained as unallocated retained earnings. The following patronage distributions were declared and paid in 2022, 2021 and 2020, respectively:

| | | | Cash Patronage | |
|---|---|---|---|---|
| **Date Declared** | **Nonqualified Allocated Retained Earnings Issued** | | **Amount** | **Date Paid (Payable)** |
| **December 2022** | **$** | **142,433** | **$ 127,595** | **March 2023** |
| December 2021 | $ | 125,700 | $ 108,069 | March 2022 |
| December 2020 | $ | 117,585 | $ 98,280 | March 2021 |

The association may create and maintain an allocated surplus account consisting of earnings held therein and allocated to borrowers on a patronage basis pursuant to its bylaws. Allocated surplus may be evidenced by either "qualified written notices of allocation" or "nonqualified written notices of allocation," or both.

All allocations in the form of qualified written notices of allocation shall be issued in annual series and shall be identified by the year of issuance. Each such series shall be retired fully or on a pro rata basis, only at the discretion of the board, in order of issuance by years as funds are available. Currently, the association has no qualified allocated equity outstanding.

All allocations in the form of nonqualified notices of allocation shall be issued in annual series and identified by the year of issuance. Each annual series may be subdivided between two or more classes. Each such series, or class thereof, shall be retired at the discretion of the board. The association currently has the following series of nonqualified allocated retained earnings outstanding, which includes adjustments made to finalize the computation of these contributions.

| Declaration for Year | Nonqualified Allocated Retained Earnings |
|---|---|
| 2014 | $ 70,065 |
| 2015 | 80,881 |
| 2016 | 77,795 |
| 2017 | 86,341 |
| 2018 | 97,044 |
| 2019 | 87,987 |
| 2020 | 117,585 |
| 2021 | 125,700 |
| 2022 | 142,433 |
| **Total** | **$ 885,831** |

In September 2022, the board of directors approved a resolution to retire $59,747 in nonqualified allocated equities that were paid to the stockholders in November 2022. The equities retired represented the remaining earnings allocated in 2013.

In September 2021, the board of directors approved a resolution to retire $60,000 in nonqualified allocated equities that were paid to the stockholders in December 2021. The equities retired represented the remaining earnings allocated in 2012 and 24 percent of the earnings allocated in 2013.

In September 2020, the board of directors approved a resolution to retire $55,000 in nonqualified allocated equities that were paid to the stockholders in November 2020. The equities retired represented 57 percent of the earnings allocated in 2012.

The Farm Credit Administration sets minimum regulatory capital requirements for banks and associations. Effective January 1, 2017, new regulatory capital requirements for banks and associations were adopted. These new requirements replaced the core surplus and total surplus requirements with Common Equity Tier 1, Tier 1 Capital and Total Capital risk-based capital ratio requirements. The new requirements also replaced the existing net collateral ratio for System banks with a Tier 1 Leverage ratio and an Unallocated Retained Earnings (URE) and URE Equivalents Leverage ratio that are applicable to both the banks and associations. The Permanent Capital Ratio continues to remain in effect; however, the risk-weighted assets are calculated differently than in the past. As of December 31, 2022, the association is not prohibited from retiring stock or distributing earnings. Furthermore, neither the board nor senior management knows of any such prohibitions that may apply during the subsequent fiscal year.

The following sets forth the regulatory capital ratio requirements and ratios at December 31, 2022:

| | **Regulatory Minimums** | **Capital Conservation Buffers*** | **Total** | **Association's ratios as of December 31, 2022** |
|---|---|---|---|---|
| Risk-adjusted: | | | | |
| Common equity tier 1 ratio | 4.50% | 2.50% * | 7.00% | 11.5% |
| Tier 1 capital ratio | 6.00% | 2.50% * | 8.50% | 13.1% |
| Total capital ratio | 8.00% | 2.50% * | 10.50% | 13.3% |
| Permanent capital ratio | 7.00% | 0.00% | 7.00% | 13.1% |
| Non-risk-adjusted: | | | | |
| Tier 1 leverage ratio** | 4.00% | 1.00% * | 5.00% | 13.9% |
| UREE leverage ratio | 1.50% | 0.00% | 1.50% | 5.4% |

*Must include the regulatory minimum requirements for the URE and UREE Leverage ratio

Risk-adjusted assets have been defined by FCA Regulation as the Statement of Condition assets and off-balance sheet commitments adjusted by various percentages, depending on the level of risk inherent in the various types of assets. The primary changes that generally have the impact of increasing risk-adjusted assets (decreasing risk-based regulatory capital ratios) were as follows:

- Inclusion of off-balance sheet commitments less than 14 months.
- Increased risk-weighting of most loans 90 days past due or in nonaccrual status.

Risk-adjusted assets is calculated differently for the permanent capital ratio compared to the other risk-based capital ratios. The primary difference is the deduction of the allowance for loan losses from risk-adjusted assets for the permanent capital ratio.

The ratios are based on a three-month average daily balance in accordance with FCA regulations and are calculated as follows:

- Common equity tier 1 ratios is statutory minimum purchased borrower stock, other required borrower stock held for a minimum of seven years, allocated equities held for a minimum of seven years or not subject to revolvement, unallocated retained earnings, paid-in capital, less certain regulatory required deductions including the amount of allocated investments in other System institutions, as the amount of purchased investments in other System institutions under the corresponding deduction approach, divided by average risk-adjusted assets.
- Tier 1 capital ratio is common equity tier 1 plus non-cumulative perpetual preferred stock, divided by average risk-adjusted assets.
- Total capital is tier 1 capital plus other required borrower stock held for a minimum of five years, allocated equities held for a minimum of five years, subordinated debt and limited-life preferred stock greater than five years to maturity at issuance subject to certain limitations, allowance and reserve for credit losses under certain limitations less certain investments in other System institutions under the corresponding deduction approach, divided by average risk-adjusted assets.
- Permanent capital ratio is all at-risk borrower stock, any allocated excess stock, unallocated retained earnings, paid-in capital, subordinated debt and preferred stock subject to certain limitations, less certain allocated and purchased investments in other System institutions, divided by risk-adjusted assets.
- Tier 1 leverage ratio is tier 1 capital, including regulatory deductions, divided by average assets less regulatory deductions subject to tier 1 capital.
- UREE leverage ratio is unallocated retained earnings, paid-in capital, allocated surplus not subject to revolvement less certain regulatory required deductions including the amount of allocated investments in other System institutions divided by average assets less regulatory deductions subject to tier 1 capital.

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

The components of the association's risk-adjusted capital, based on 90-day average balances, were as follows at December 31, 2022:

| (dollars in thousands) | Common Equity Tier 1 Ratio | Tier 1 Capital Ratio | Total Capital Ratio | Permanent Capital Ratio |
|---|---|---|---|---|
| Numerator: | | | | |
| Unallocated retained earnings | $ 784,661 | $ 784,661 | $ 784,661 | $ 784,661 |
| Common Cooperative Equities: | | | | |
| Statutory minimum purchased borrower stock | 28,484 | 28,484 | 28,484 | 28,484 |
| Allocated equities held ≥seven years | 758,259 | 758,259 | 758,259 | 758,259 |
| Nonqualified allocated equities not subject to retirement | - | | | |
| Non-cumulative perpetual preferred stock | - | 200,000 | 200,000 | 200,000 |
| Allowance for loan losses and reserve for credit losses subject to certain limitations* | - | - | 26,693 | - |
| Regulatory Adjustments and Deductions: | | | | |
| Amount of allocated investments in other System institutions | (160,287) | (160,287) | (160,287) | (160,287) |
| Other regulatory required deductions | (1,391) | (1,391) | (1,391) | (1,391) |
| | **$ 1,409,726** | **$ 1,609,726** | **$ 1,636,419** | **$ 1,609,726** |
| Denominator: | | | | |
| Risk-adjusted assets excluding allowance | $ 12,436,936 | $ 12,436,936 | $ 12,436,936 | $ 12,436,936 |
| Regulatory Adjustments and Deductions: | | | | |
| Regulatory deductions included in total capital | (161,678) | (161,678) | (161,678) | (161,678) |
| Allowance for loan losses | | | | (26,337) |
| | **$ 12,275,258** | **$ 12,275,258** | **$ 12,275,258** | **$ 12,248,921** |

*Capped at 1.25% of risk-adjusted assets

The components of the association's non-risk-adjusted capital, based on 90 average balances, were as follows at December 31, 2022:

| | Tier 1 Leverage Ratio | UREE Leverage Ratio |
|---|---|---|
| Numerator: | | |
| Unallocated retained earnings | $ 784,661 | $ 784,661 |
| Statutory minimum purchased borrower stock | 28,484 | - |
| Allocated equities held ≥seven years | 758,259 | - |
| Non-cumulative perpetual preferred stock | 200,000 | - |
| Regulatory Adjustments and Deductions: | | |
| Amount of allocated investments in other System institutions | (160,287) | (160,287) |
| Other regulatory required deductions | (1,391) | (1,391) |
| | **$ 1,609,726** | **$ 622,983** |
| Denominator: | | |
| Total Assets | $ 11,815,305 | $ 11,815,305 |
| Regulatory Adjustments and Deductions: | | |
| Regulatory deductions included in tier 1 capital | (209,578) | (209,578) |
| | **$ 11,605,727** | **$ 11,605,727** |

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

At December 31, the association did not have shares of Class A capital stock, but it did have the following shares of Class B stock and participation certificates outstanding at a par value of $5 dollars per share:

| | **2022** | 2021 | 2020 |
|---|---|---|---|
| Class B stock | **5,408** | 5,401 | 5,150 |
| Participation certificates | **259** | 281 | 259 |
| Total | **5,667** | 5,682 | 5,409 |

The association’s accumulated other comprehensive income (loss) relates entirely to its non-pension other postretirement benefits. The following table summarizes the changes in accumulated other comprehensive income (loss) and the location on the income statement for the year ended December 31:

| | **2022** | 2021 | 2020 |
|---|---|---|---|
| Accumulated other comprehensive (loss) at January 1 | **$ (2,957)** | $ (3,557) | $ (2,923) |
| Actuarial gains (losses) | **6,219** | 555 | (621) |
| Prior service (cost) credit | **-** | - | - |
| Amortization of prior service (credit) included in salaries and employee benefits | **(183)** | (183) | (183) |
| Amortization of actuarial gain included in salaries and employee benefits | **114** | 228 | 170 |
| Income tax expense related to items of other comprehensive income | **-** | - | - |
| Other comprehensive gain (loss), net of tax | **6,150** | 600 | (634) |
| Accumulated other comprehensive income (loss) at December 31 | **$ 3,193** | $ (2,957) | $ (3,557) |

**NOTE 12 — INCOME TAXES:**

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

| | **2022** | 2021 | 2020 |
|---|---|---|---|
| Current federal tax | **$ (1)** | $ 50 | $ - |
| Deferred federal tax | **-** | - | - |
| (Benefit from)/provision for income taxes | **$ (1)** | $ 50 | $ - |

The association has a net operating loss carryforward of $21,696 available to offset against future taxable income of which $1,039 will expire in 2024, $1,811 will expire in 2025, $8,512 will expire in 2029 and $10,334 will expire in 2030.

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

| | **2022** | 2021 | 2020 |
|---|---|---|---|
| Federal tax at statutory rate | **$ 60,125** | $ 54,970 | $ 46,254 |
| Federal income tax attributable to: | | | |
| Income not subject to federal tax | **(55,378)** | (51,459) | (43,425) |
| Nondeductible provision for loan losses | **(161)** | (788) | (324) |
| Patronage distributions | **(4,628)** | (2,775) | (2,442) |
| Recoveries (charge-offs) on loans | **45** | 56 | (10) |
| Other | **(4)** | 46 | (53) |
| Provision for (Benefit from) income taxes | **$ (1)** | $ 50 | $ - |

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

| | **2022** | 2021 | 2020 |
|---|---|---|---|
| Allowance for losses on loans | **$ 1,580** | $ 1,696 | $ 2,427 |
| Net operating loss carryforward | **4,556** | 4,556 | 4,502 |
| Deferred tax assets | **6,136** | 6,252 | 6,929 |
| Valuation allowance | **(6,136)** | (6,252) | (6,929) |
| Net deferred tax asset | **$ -** | $ - | $ - |

The calculation of tax assets and liabilities involves various management estimates and assumptions as to the future taxable earnings. At December 31, 2022, non-patronage income is expected to be less than 5 percent of total taxable income (before patronage) and all patronage income is expected to be disbursed over time. The expected future tax rates are based upon enacted tax laws.

The association recorded valuation allowances of $6,136, $6,252 and $6,929 during 2022, 2021 and 2020, respectively. The association will continue to evaluate the realizability of the deferred tax assets and adjust the valuation allowance accordingly. The association follows FASB guidance on accounting for uncertainty in income taxes. At December 31, 2022, 2021 and 2020, the association did not recognize a tax liability for any uncertain tax positions.

## NOTE 13 — EMPLOYEE BENEFIT PLANS:

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

The CEO and certain members of senior management or highly compensated employees in the association are eligible to participate in a separate nonqualified supplemental 401(k) plan, named the Farm Credit Benefits Alliance Nonqualified Supplemental 401(k) Plan (Supplemental 401(k) Plan). This plan allows district employers to elect to participate in any or all the following benefits:

- Restored Employer Contributions – to allow "make up" contributions for eligible employees whose benefits to the qualified 401(k) plan were limited by the Internal Revenue Code during the year.
- Elective Deferrals – to allow eligible employees to make pre-tax deferrals of compensation above and beyond any deferrals into the qualified 401(k) plan.
- Discretionary Contributions – to allow participating employers to make a discretionary contribution to an eligible employee's account in the plan and to designate a vesting schedule.

The association elected to participate in the Supplemental 401(k) Plan and provided for elective deferrals and discretionary contributions to be made through the plan. The total expenses of the nonqualified plan included in the association's employee benefit costs were $144, $617 and $864 for the years ended December 31, 2022, 2021 and 2020, respectively.

| Plan Name | Farm Credit Benefits Alliance Nonqualifed Supplemental 401(k) Plan |
|---|---|
| Present Value of accumulated benefits | **$8,339** |
| Contributions made during the year | **$144** |
| Distributions made during the year | **--** |
| Funded obligations | **$8,339** |
| Off-balance sheet amounts including benefits earned but not vested | **None** |

The DB plan is noncontributory, and benefits are based on salary and years of service. The legal name of the plan is the Farm Credit Bank of Texas Pension Plan; its employer identification number is 74-1110170. The DB plan is not subject to any contractual expiration dates. The DB plan's funding policy is to fund current year benefits expected to be earned by covered employees plus an amount to improve the accumulated benefit obligation funded status by the percentage approved by the plan sponsor. The plan sponsor is the board of directors of the Farm Credit Bank of Texas. The "projected unit credit" actuarial method is used for both financial reporting and funding purposes. District employers have the option of providing enhanced retirement benefits, under certain conditions, within the DB plan, to facilitate reorganization and/or restructuring. The actuarial present value of vested and nonvested accumulated benefit obligations exceeded the net assets of the DB plan as of December 31, 2022.

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

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

The following table includes additional information regarding the funded status of the plan, the association's contributions, and the percentage of association contribution to total plan contributions for the years ended December 31, 2022, 2021 and 2020:

| | 2022 | 2021 | 2020 |
|---|---|---|---|
| Funded status of plan | **70.9%** | 70.5% | 62.6% |
| Association's contribution | **$ 3,083** | $ 4,376 | $ 1,834 |
| Percentage of association's contribution to total contributions | **29.6%** | 28.9% | 30.4% |

The funded status presented above is based on the percentage of plan assets to projected benefit obligations. DB plan funding is based on the percentage of plan assets to the accumulated benefit obligation, which was 71.8 percent, 72.0 percent and 64.3 percent at December 31, 2022, 2021 and 2020, respectively.

**Other Postretirement Benefits**: In addition to pension benefits, the association provides certain health care benefits to qualifying retired employees (other postretirement benefits) for those employees hired on or before December 31, 2003. These benefits are not characterized as multiemployer and, consequently, the liability for these benefits is included in the liability section of the association's consolidated balance sheet. Association employees hired after January 1, 2004, will be eligible for retiree medical benefits for themselves and their spouses but will be responsible for 100 percent of the related premiums.

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

**Retiree Welfare Benefit Plans**

| | 2022 | 2021 | 2020 |
|---|---|---|---|
| **Change in Accumulated Postretirement Benefit Obligation** | | | |
| Accumulated postretirement benefit obligation, beginning of year | **$ 27,286** | $ 27,472 | $ 26,300 |
| Service cost | **358** | 382 | 401 |
| Interest cost | **846** | 757 | 895 |
| Plan participants' contributions | **226** | 185 | 178 |
| Plan amendments | **-** | - | - |
| Actuarial (Gain) loss | **(6,219)** | (555) | 621 |
| Benefits paid | **(1,077)** | (955) | (923) |
| Accumulated postretirement benefit obligation, end of year | **$ 21,420** | $ 27,286 | $ 27,472 |
| **Change in Plan Assets** | | | |
| Association contributions | **$ 851** | $ 770 | $ 745 |
| Plan participants' contributions | **226** | 185 | 178 |
| Benefits paid | **(1,077)** | (955) | (923) |
| Plan assets at fair value, end of year | **$ -** | $ - | $ - |
| Funded status of the plan | **$ (21,420)** | $ (27,286) | $ (27,472) |
| **Amounts Recognized in Consolidated Balance Sheet** | | | |
| Current liabilities | **$ (958)** | $ (944) | $ (859) |
| Noncurrent liabilities | **(20,462)** | (26,342) | (26,613) |
| Total | **$ (21,420)** | $ (27,286) | $ (27,472) |
| **Amounts Recognized in Accumulated Other Comprehensive Income (AOCI)** | | | |
| Net actuarial (gain)/loss | **$ (2,871)** | $ 3,461 | $ 4,245 |
| Prior service credit | **(322)** | (504) | (688) |
| Total | **$ (3,193)** | $ 2,957 | $ 3,557 |
| **Weighted-Average Assumptions Used to Determine Obligations at Year End** | | | |
| Measurement date | **12/31/2022** | 12/31/2021 | 12/31/2020 |
| Discount rate | **5.20%** | 3.15% | 2.80% |
| Health care cost trend rate assumed for next year (pre-/post-65) | **7.20%/7.70%** | 6.80%/6.00% | 6.90%/6.40% |
| Ultimate health care cost trend rate | **4.50%** | 4.50% | 4.50% |
| Year that the rate reaches the ultimate trend rate | **2031/2031** | 2030/2030 | 2028/2029 |

| Disclosure Information Related to Retirement Benefits | 2022 | 2021 | 2020 |
|---|---|---|---|
| **Components of Net Postretirement Benefit Cost** | | | |
| Service Cost | **$ 358** | $ 382 | $ 401 |
| Interest cost | **846** | 757 | 895 |
| Amortization of: | | | |
| Prior service credit | **(183)** | (183) | (183) |
| Actuarial loss | **114** | 228 | 170 |
| Net postretirement benefit cost | **$ 1,135** | $ 1,184 | $ 1,283 |
| | | | |
| **Other Changes in Plan Assets and Benefit Obligation Recognized in Other Comprehensive Income** | | | |
| Net actuarial (gain) loss | **$ (6,219)** | $ (555) | $ 621 |
| Amortization of: | | | |
| Prior service credit | **183** | 183 | 183 |
| Net actuarial (loss) | **(114)** | (228) | (170) |
| Total recognized in other comprehensive (income) loss | **$ (6,150)** | $ (600) | $ 634 |
| | | | |
| **AOCI Amounts Expected to be Amortized into Expense** | | | |
| Prior service credit | **$ (183)** | $ (183) | $ (183) |
| Net actuarial (gain)/loss | **(110)** | 114 | 228 |
| Total | **$ (293)** | $ (69) | $ 45 |
| | | | |
| **Weighted-Average Assumptions Used to Determine Net Postretirement Benefit Cost** | | | |
| Measurement date | **12/31/2021** | 12/31/2020 | 12/31/2019 |
| Discount rate | **3.15%** | 2.80% | 3.45% |
| Health care cost trend rate assumed for next year (pre-/post-65) | **6.80%/6.00%** | 6.60/6.20% | 6.90%/6.40% |
| Ultimate health care cost trend rate | **4.50%** | 4.50% | 4.50% |
| Year that the rate reaches the ultimate trend rate | **2030** | 2029 | 2028 |

**Expected Future Cash Flows**

| Expected Benefit Payments (net of employee contributions) | |
|---|---|
| Fiscal 2023 | **$ 957** |
| Fiscal 2024 | **1,018** |
| Fiscal 2025 | **1,041** |
| Fiscal 2026 | **1,132** |
| Fiscal 2027 | **1,192** |
| Fiscal 2028 to 2032 | **6,579** |
| | |
| **Expected Contributions** | |
| Fiscal 2023 | **$ 957** |

## NOTE 14 — RELATED PARTY TRANSACTIONS:

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

Total loans to such persons for the association amounted to $66,560, $23,348 and $24,458 at December 31, 2022, 2021 and 2020, respectively. During 2022, 2021 and 2020, $237,464, $24,611 and $19,209 of new loans were made and repayments totaled $194,252, $25,721 and $18,980, respectively. These balances do not include sold loans. In the opinion of management, no such loans outstanding at December 31, 2022, 2021 and 2020, involved more than a normal risk of collection.

Expenses included in purchased services and data processing may include purchased services such as administrative services, marketing, information systems and accounting services and allocations of expenses incurred by the bank and passed through to the associations, such as FCSIC expenses. The bank charges the individual associations directly for these services based on each association's proportionate usage. These expenses totaled $2,331, $2,063 and $1,659 in 2022, 2021 and 2020, respectively

The association received patronage income from the bank totaling $71,109, $59,185 and $48,940 during 2022, 2021 and 2020, respectively.

**NOTE 15 — FAIR VALUE MEASUREMENTS:**

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

Assets measured at fair value on a recurring basis, which are measured at fair value at the end of each reporting period on the association's consolidated balance sheet, at December 31, 2022, 2021 and 2020 for each of the fair value hierarchy values are summarized below. The association did not have any liabilities measured at fair value on a recurring basis.

| **December 31, 2022** | **Fair Value Measurement Using** | | | **Total Fair** |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Value** |
| Assets: | | | | |
| Assets held in nonqualified benefit trusts | **$ 8,339** | **$ -** | **$ -** | **$ 8,339** |
| Total assets | **$ 8,339** | **$ -** | **$ -** | **$ 8,339** |

| December 31, 2021 | Fair Value Measurement Using | | | Total Fair |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Value |
| Assets: | | | | |
| Assets held in nonqualified benefit trusts | $ 11,121 | $ - | $ - | $ 11,121 |
| Total assets | $ 11,121 | $ - | $ - | $ 11,121 |

| December 31, 2020 | Fair Value Measurement Using | | | Total Fair |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Value |
| Assets: | | | | |
| Assets held in nonqualified benefit trusts | $ 9,365 | $ - | $ - | $ 9,365 |
| Total assets | $ 9,365 | $ - | $ - | $ 9,365 |

Assets measured at fair value on a nonrecurring basis, which are fair value measurements that are triggered by particular circumstances such as impaired assets, for each of the fair value hierarchy values are summarized below. The association did not have any liabilities measured at fair value on a nonrecurring basis.

| **December 31, 2022** | **Fair Value Measurement Using** | | | **Total Fair** |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Value** |
| Assets: | | | | |
| Loans* | **$ -** | **$ -** | **$ 19,424** | **$ 19,424** |
| Other property owned | **-** | **-** | **3,358** | **3,358** |

| December 31, 2021 | Fair Value Measurement Using | | | Total Fair |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Value |
| Assets: | | | | |
| Loans* | $ - | $ - | $ 12,777 | $ 12,777 |
| Other property owned | - | - | 1,704 | 1,704 |

| December 31, 2020 | Fair Value Measurement Using | | | Total Fair |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Value |
| Assets: | | | | |
| Loans* | $ - | $ - | $ 9,535 | $ 9,535 |
| Other property owned | - | - | 627 | 627 |

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

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

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

| | **December 31, 2022** | | | | |
|---|---|---|---|---|---|
| | **Total Carrying Amount** | **Level 1** | **Level 2** | **Level 3** | **Total Fair Value** |
| Assets: | | | | | |
| Cash | **$ -** | **$ -** | **$ -** | **$ -** | **$ -** |
| Mission-related and other investments held-to-maturity | **1,496** | **-** | **-** | **1,427** | **1,427** |
| Net loans | **11,447,015** | **-** | **-** | **10,616,129** | **10,616,129** |
| Total Assets | **$ 11,448,511** | **$ -** | **$ -** | **$ 10,617,556** | **$ 10,617,556** |
| Liabilities: | | | | | |
| Note payable to the Bank | **9,840,475** | **-** | **-** | **9,127,431** | **9,127,431** |
| Total Liabilities | **$ 9,840,475** | **$ -** | **$ -** | **$ 9,127,431** | **$ 9,127,431** |

| | December 31, 2021 | | | | |
|---|---|---|---|---|---|
| | Total Carrying Amount | Level 1 | Level 2 | Level 3 | Total Fair Value |
| Assets: | | | | | |
| Cash | $ - | $ - | $ - | $ - | $ - |
| Mission-related and other investments held-to-maturity | 1,952 | - | - | 2,001 | 2,001 |
| Net loans | 10,420,738 | - | - | 10,451,092 | 10,451,092 |
| Total Assets | $ 10,422,690 | $ - | $ - | $ 10,453,093 | $ 10,453,093 |
| Liabilities: | | | | | |
| Note payable to the Bank | 8,873,812 | - | - | 8,899,615 | 8,899,615 |
| Total Liabilities | $ 8,873,812 | $ - | $ - | $ 8,899,615 | $ 8,899,615 |

| | December 31, 2020 | | | | |
|---|---|---|---|---|---|
| | Total Carrying Amount | Level 1 | Level 2 | Level 3 | Total Fair Value |
| Assets: | | | | | |
| Cash | $ 2 | $ 2 | $ - | $ - | $ 2 |
| Mission-related and other investments held-to-maturity | 2,582 | - | - | 2,648 | 2,648 |
| Net loans | 8,643,004 | - | - | 8,836,797 | 8,836,797 |
| Total Assets | $ 8,645,588 | $ 2 | $ - | $ 8,839,445 | $ 8,839,447 |
| Liabilities: | | | | | |
| Note payable to the Bank | 7,374,054 | - | - | 7,538,853 | 7,538,853 |
| Total Liabilities | $ 7,374,054 | $ - | $ - | $ 7,538,853 | $ 7,538,853 |

**Valuation Techniques**

As more fully discussed in Note 2, "Summary of Significant Accounting Policies," accounting guidance establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. Fair values of financial instruments represent the estimated amount to be received to sell an asset or paid to transfer or extinguish a liability in active markets among willing participants at the reporting date. Due to the uncertainty of expected cash flows resulting from financial instruments, the use of different assumptions and valuation methodologies could significantly affect the estimated fair value amounts. Accordingly, certain of the estimated fair values may not be indicative of the amounts for which the financial instruments could be exchanged in a current or future market transaction. The following represent a brief summary of the valuation techniques used by the association for assets and liabilities:

| | Valuation Technique(s) | Input |
|---|---|---|
| Cash | Carrying value | Par/principal and appropriate interest yield |
| Investments held-to-maturity | Discounted cash flow | Prepayment rates<br>Probability of default<br>Loss severity |
| Loans | Discounted cash flow | Prepayment forecasts<br>Probability of default<br>Loss severity |
| Other interest bearing liabilities | Carrying value | Par/principal and appropriate interest yield |
| Other property owned | Carrying value | Each collateral property is unique |

Information About Level 3 Fair Value Measurements

| | Valuation Technique(s) | Unobservable Input | Range of Inputs |
|---|---|---|---|
| Investments held-to-maturity | Discounted cash flow | Prepayment rates | 3.0% - 32.1% |

**A. Cash:**

For cash, the carrying amount is a reasonable estimate of fair value. The fair value of term federal funds sold and securities purchased under resale agreements is based on currently quoted market prices, which are reflective of current interest rates.

**B. Investment Securities:**

Include mortgage-backed securities issued by the Federal Agricultural Mortgage Corporation (Farmer Mac). Fair values are estimated using discounted cash flows considering market interest rates, estimated prepayment rates, probabilities of default and loss severities. Inputs depend significantly on management judgments and experience with the securities. These fair value measurements are classified as level 3 investments.

**C. Loans Evaluated for Impairment:**

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

**D. Assets Held in Nonqualified Benefits Trusts:**

Assets held in nonqualified benefits trusts related to deferred compensation and supplemental retirement plans are classified as Level 1. Level 1 valuation utilizes quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. The trust funds include investments that are actually traded and have quoted net asset values that are quoted in the marketplace.

**E. Standby Letters of Credit:**

The fair value of letters of credit approximate the fees currently charged for similar agreements or the estimated cost to terminate or otherwise settle similar obligations.

**F. Other Property Owned:**

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

**G. Note Payable to the Bank:**

The note payable to the bank is not regularly traded; thus, quoted market prices are not available. Fair value of this instrument is discounted based on the association's and bank's loan rates as well as on management estimates. For the purposes of this estimate it is assumed that the cash flow on the note is equal to the principal payments on the association's loan receivables plus accrued interest on the note payable. This assumption implies that earnings on the association's interest margin are used to fund operating expenses and capital expenditures. Management has no basis to determine whether the fair values would be indicative of the value negotiated in an actual sale.

## NOTE 16 — COMMITMENTS AND CONTINGENCIES:

In addition to those commitments and contingencies discussed in Note 2, "Summary of Significant Accounting Policies," the association is involved in various legal proceedings in the ordinary course of business. In the opinion of legal counsel and management, there are no legal proceedings at this time that are likely to materially affect the association.

The association may participate in financial instruments with off-balance sheet risk to satisfy the financing needs of its borrowers in the form of commitments to extend credit and letters of credit. These financial instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the financial statements. Commitments to extend credit are agreements to lend to a borrower as long as there is not a violation of any condition established in the contract. Commercial letters of credit are agreements to pay a beneficiary under conditions specified in the letter of credit. Commitments and letters of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee by the borrower. At December 31, 2022, the association had $1,792,459 of commitments to extend credit and $23,852 of letters of credit were outstanding.

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

The association also participates in standby letters of credit to satisfy the financing needs of its borrowers. These letters of credit are irrevocable agreements to guarantee payments of specified financing obligations. Standby letters of credit are recorded, at fair value, on the balance sheet by the association. At December 31, 2022, there were no standby letters of credit included in other liabilities. Outstanding standby letters of credit have expiration dates ranging from January 2, 2023, to November 6, 2026. The maximum potential amount of future payments the association is required to make under the guarantees is $23,852.

## NOTE 17 – QUARTERLY FINANCIAL INFORMATION (UNAUDITED):

Quarterly results of operations for the years ended December 31 are as follows:

| | 2022 | | | | |
|---|---|---|---|---|---|
| | **First** | **Second** | **Third** | **Fourth** | **Total** |
| **Net interest income** | **$ 77,704** | **$ 79,054** | **$ 82,009** | **$ 84,032** | **$ 322,799** |
| **Reversal of (provision for) loan losses** | **1,836** | **(948)** | **(4,017)** | **4,132** | **1,003** |
| **Noninterest expense, net** | **(9,304)** | **(8,978)** | **(10,186)** | **(9,025)** | **(37,493)** |
| **Net income** | **$ 70,236** | **$ 69,128** | **$ 67,806** | **$ 79,139** | **$ 286,309** |

| | 2021 | | | | |
|---|---|---|---|---|---|
| | First | Second | Third | Fourth | Total |
| Net interest income | $ 66,344 | $ 68,598 | $ 71,328 | $ 74,130 | $ 280,400 |
| Reversal of (provision for) loan losses | 4,894 | 3,011 | 138 | 1,155 | 9,198 |
| Noninterest expense, net | (3,431) | (8,773) | (8,954) | (6,727) | (27,885) |
| Net income | $ 67,807 | $ 62,836 | $ 62,512 | $ 68,558 | $ 261,713 |

| | 2020 | | | | |
|---|---|---|---|---|---|
| | First | Second | Third | Fourth | Total |
| Net interest income | $ 60,418 | $ 60,530 | $ 62,505 | $ 64,189 | $ 247,642 |
| (Provision for) reversal of loan losses | (14) | (549) | (4,455) | 4,436 | (582) |
| Noninterest expense, net | (9,852) | (6,667) | (5,985) | (4,298) | (26,802) |
| Net income | $ 50,552 | $ 53,314 | $ 52,065 | $ 64,327 | $ 220,258 |

## NOTE 18 – SUBSEQUENT EVENTS:

The association has evaluated subsequent events through March 9, 2023, which is the date the financial statements were issued or available to be issued and has determined that there were no other events requiring disclosure.

## DISCLOSURE INFORMATION AND INDEX

(Unaudited)

*Disclosures Required by Farm Credit Administration Regulations*

### DESCRIPTION OF BUSINESS

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

The descriptions of significant developments that had or could have a material impact on earnings or interest rates to borrowers, patronage or dividends and acquisitions or dispositions of material assets, if any, required to be disclosed in this section are incorporated herein by reference to “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” included in this annual report.

### DESCRIPTION OF PROPERTY

Capital Farm Credit, ACA (the association) serves its 192-county territory through its main administrative office at 3000 Briarcrest Drive, Suite 601, Bryan, Texas, and through its accounting/administration, agri-insurance, loan processing/review, special assets and marketing/operations offices, which are in Amarillo, Boerne, Bryan, Devine, Hondo, Lubbock, and Round Rock, Texas. Additionally, there are 67 lending offices located throughout the territory. The association owns the office buildings in Alpine, Bellville, Bowie, Canadian, Childress, Clifton, Crosbyton, Dalhart, Dayton, Dimmitt, Edna, El Campo, Goldthwaite, Hereford, Hondo, Jourdanton, Kenedy, Kerrville, La Grange, Lamesa, Levelland, Littlefield, Lockhart, Madisonville, Mason, Matador, Muleshoe, Munday, Pampa, Perryton, Rosenberg, San Saba, Snyder, Sonora, Spur, Taylor, Temple, Uvalde, Vernon, Wheeler and Wichita Falls, free of debt. The association leases office buildings in Abilene, Amarillo, Austin, Bay City, Boerne, Brenham, Bryan, Burnet, Conroe, Crockett, Devine, Edinburg, El Paso, Fredericksburg, Harlingen, Hondo, Katy, La Grange, Laredo, Livingston, Lubbock, New Braunfels, Robstown, Round Rock, San Angelo, San Antonio, Seminole, Stamford, Victoria, Waco and Winnie, Texas.

In 2022, the association sold buildings in Tulia and in Stamford. New leases were entered into for office locations in New Braunfels, Seminole, Katy, Amarillo, and Stamford. The association renewed leases in Alpine, Winnie, La Grange, Laredo, Conroe, Katy, Burnet, Abilene and Fredericksburg. During 2022, the association closed the Crosbyton, Goldthwaite, Sonora and Wheeler offices and consolidated them into Lubbock, San Saba, San Angelo and Pampa, respectively.

In 2021, the association sold its buildings in San Angelo and Waco and entered into new leases for both locations. Additionally, new leases were entered into for new office locations in Brenham and Victoria, and the association entered a new lease in Hondo. The association renewed leases in Abilene, Austin, Burnet, Bay City, Devine, New Braunfels, La Grange, Lubbock, Winnie and Seminole.

In 2020, the association renewed leases in Hondo, Winnie, Crockett, Livingston, New Braunfels, Austin, Fredericksburg, Katy and Harlingen.

### LEGAL PROCEEDINGS

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

### DESCRIPTION OF CAPITAL STRUCTURE

The information required to be disclosed in this section is incorporated herein by reference to Note 11 to the consolidated financial statements, “Members’ Equity,” included in this annual report.

## DESCRIPTION OF LIABILITIES

The description of liabilities required to be disclosed in this section is incorporated herein by reference from Note 10 to the consolidated financial statements, "Note Payable to the Bank," Note 13, "Employee Benefit Plans" and in "Management's Discussion and Analysis of Financial Condition and Results of Operations," included in this annual report. The description of contingent liabilities required to be disclosed in this section is incorporated herein by reference from Notes 2 and 16 to the consolidated financial statements, "Summary of Significant Accounting Policies" and "Commitments and Contingencies," respectively, included in this annual report.

## RELATIONSHIP WITH THE FARM CREDIT BANK OF TEXAS

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

The bank's annual and quarterly stockholder reports are available free of charge, upon request. These reports can be obtained by writing to Farm Credit Bank of Texas, Corporate Communications, P.O. Box 202590, Austin, Texas 78720-2590 or calling (512) 465-1881. Copies of the bank's annual and quarterly stockholder reports can also be requested by emailing *fcb@farmcreditbank.com*. The annual and quarterly stockholder reports are also available on the bank's website at www.farmcreditbank.com.

The association's quarterly stockholder reports are also available free of charge, upon request. These reports will be available approximately 40 days after quarter end and can be obtained by writing to Capital Farm Credit, P.O. Box 488, Hondo, Texas 78861 or calling (830) 426-4589. Copies of the association's quarterly stockholder reports can also be requested by emailing *Javier.Lemus@capitalfarmcredit.com*. The association's annual stockholder report is available on its website at *www.capitalfarmcredit.com* 75 days after the year end. Copies of the association's annual stockholder report can also be requested 90 days after the year end.

## SELECTED FINANCIAL DATA

The selected financial data for the five years ended December 31, 2022, required to be disclosed, is incorporated herein by reference to the "Five-Year Summary of Selected Consolidated Financial Data" included in this annual report to stockholders.

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

"Management's Discussion and Analysis," which precedes the consolidated financial statements in this annual report, is incorporated herein by reference.

## DIRECTORS AND SENIOR OFFICERS

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

| NAME | POSITION | ELECTED/ TIME IN POSITION | TERM EXPIRES |
|---|---|---|---|
| John Malazzo | Chairman & Stockholder-Elected Director | 2007 | 2023 |
| Kenton B. Kimball | Vice-Chairman and Stockholder-Elected Director | 2000 | 2023 |
| Paul Aelvoet | Stockholder-Elected Director | 2000 | 2026 |
| Jim Brock | Director-Elected Director | 2022 | 2026 |
| Kenny Brown | Stockholder-Elected Director | 2021 | 2025 |
| Dale Crenwelge | Stockholder-Elected Director | 2008 | 2025 |
| Rachel Cutrer | Stockholder-Elected Director | 2022 | 2026 |
| Josh Eilers | Stockholder-Elected Director | 2021 | 2025 |
| Kelly Gaskins* | Stockholder-Elected Director | 2001 | 2022 |
| Dale Hoelscher | Stockholder-Elected Director | 2009 | 2023 |
| Jerred Hurst | Director-Elected Director | 2018 | 2026 |
| Terry McAlister | Stockholder-Elected Director | 1992 | 2026 |
| Josh McDonald | Stockholder-Elected Director | 2022 | 2026 |
| Lance D. Morris | Stockholder-Elected Director | 1988 | 2023 |
| Gary L. Palousek | Stockholder-Elected Director | 2003 | 2023 |
| Danny Parker | Stockholder-Elected Director | 1998 | 2025 |
| Ronnie Riddle | Stockholder-Elected Director | 2012 | 2024 |
| Shane Sklar | Stockholder-Elected Director | 2020 | 2024 |
| Steve Stevens* | Director-Elected Director | 2017 | 2024 |
| Sharleen Walkoviak | Director-Elected Director | 2018 | 2026 |
| Lowell Woodward | Stockholder-Elected Director | 2005 | 2026 |
| Joe David Yates* | Stockholder-Elected Director | 2018 | 2022 |
| Jeff Norte | President & Chief Executive Officer | 2021 | ---- |
| Chris Burt | Chief Human Resources Officer | 2021 | ---- |
| Jon Hutchinson | Chief Credit Officer | 2021 | ---- |
| Sally Lawson | Chief Financial Officer | 2021 | ---- |
| Phil Peabody | Chief Lending Officer | 2021 | ---- |
| Wes Sutton | General Counsel | 2018 | ---- |
| Jennifer Thompson | Chief Administrative Officer | 2022 | ---- |
| Glenn Trant | Chief Operating Officer | 2021 | ---- |

Director-Elected Director: a director-appointed director who is not a stockholder, director, officer, employee or agent of a Farm Credit System institution (other than as an outside director of the association or its subsidiaries).

*Denotes board members who served during 2022 but will not continue in 2023

A brief statement of the business and employment background of each director and senior officer as of December 31, 2022 is provided for informational purposes.

**John Malazzo** raises cotton and corn and has a cattle production operation in Brazos and Burleson counties, Texas. Mr. Malazzo resides in Caldwell, Texas. Mr. Malazzo also serves on the board of Producers Co-op of Bryan, Texas, which provides agricultural goods and services to farmers and ranchers.

**Kenton B. Kimball** farms and ranches in Stratford, Texas. Mr. Kimball is the owner and president of Kimball Cattle Inc., a farming and cattle business with current operations in northeast Oklahoma. Mr. Kimball has also owned and managed agricultural operations in Sherman County, Texas, in the past.

**Paul Aelvoet** is a self-employed farmer/rancher in Medina County, Texas, and resides in Hondo, Texas. He is managing partner of Aelvoet Partners and of D/A Cattle Co, which are farming and ranching operations. Mr. Aelvoet serves as co-chairman of the Hondo 4H Booster Club.

**Jim Brock** has extensive experience serving as a board member for many organizations throughout his career. Mr. Brock currently serves as the managing, founding member of TBR Advisors, LLC in Houston, Texas, a business advisory services company that provides support and advice for organizations facing operation and financial challenges.

**Kenny Brown** has completed a career that has spanned 32 years in the Farm Credit System, retired from Capital Farm Credit in March of 2018. During these 32 years, he served as an examiner with the Farm Credit Administration, a lending officer with Heritage Land Bank in Tyler, Texas, and spent 17 years prior to retirement with Capital Farm Credit. Mr. Brown maintains a cattle operation in western Coryell County. He has served as a consultant with multiple Farm Credit institutions in Texas and New Mexico since retirement. He is a member of the Coryell County Farm Bureau.

**Dale Crenwelge** resides in Comfort, Kerr County, Texas, and his principal occupation is ranching and real estate investment and development. Mr. Crenwelge's business interests include serving as president or general partner of Grobe-Lich Properties LTD, GrobeLich Properties LLC, DKBC I LTD, DKBC II LTD, Pine Ridge Developers LLC, Oak Creek/Mopac Self Storage LP, Crenwelge LLC, Port Aransas Ventures 7, Austin Mini Storage, Vega Altamesa Self Storage LP, D and D Terrell County Ranch Partnership, Dancing Hill, LLC, and Dale and Daniel F. Crenwelge. Mr. Crenwelge serves on the board of Hill Country Memorial Hospital in Fredericksburg, Texas, as chairman of Audit/Finance Committee to Kerr County 4-H Foundation, and as a trustee of Centurions of Kendall County.

**Rachel Cutrer** is a seventh-generation Texas rancher and businesswoman from Wharton County. In 1999, she created Ranch House Designs, the world leader in livestock marketing, and has served as CEO since its inception. Cutrer is also co-owner of B.R. Cutrer Ranch, one of the world's leading Brahman cattle operations, and a founder and partner of Brahman Country Beef, Brahman Country Genetics, FitBeef, and The Ranch Downtown.

**Josh Eilers** is a former United States Army Ranger and has been the owner and operator of Ranger Cattle for the past 10 years. After being awarded a Purple Heart for wounds sustained in combat, Mr. Eilers transitioned from the military to agriculture. Mr. Eilers' livestock production consists of raising high-quality Wagyu beef in Travis County, Texas, from conception to consumption and managing a co-op network of producers from the panhandle of Texas across the southeast United States.

**Kelly Gaskins** resides in Shamrock, Wheeler County, Texas, and is a self-employed owner of agricultural and pipeline construction businesses that operate under the names of Gaskins Double G Corp, Hoptoad Enterprises Inc., Salt Cedar Farms Inc., KG Farm Services Inc., Circle TK Land & Cattle, and Kelly Gaskins Farms Inc.

**Dale Hoelscher** farms and ranches in Bell, Falls, Milam, and Robertson counties, and resides in Bell County, Texas. He primarily grows corn and cotton and also has a cow/calf operation. Mr. Hoelscher's business interests include Hoelscher Brothers Farm and R&D Hoelscher Farm LLC, a farming and ranching operation. His other business interests include D&M Grain, Producers Coop, and B.F. & M. Coop.

**Jerred Hurst** resides in Lubbock, Lubbock County, Texas and is the chief technology officer (CTO) for Primitive Social, a digital agency specializing in web design and development, branding, inbound marketing and social media. In addition, he is a founder for nSpire Labs, a stockholder and CTO for Hurst Farm Supply, a leading equipment dealership in West Texas, CTO and co-owner of Fastpay Payroll, which provides companies with payroll solutions, and co-owner of Elevate Accounting.

**Terry McAlister** resides in Electra, Texas, and farms and ranches in Wichita and Wilbarger counties. Mr. McAlister is president and CEO of McAlister Properties Inc. He serves as an appointed representative of the Wichita County Boll Weevil Eradication Foundation.

**Josh McDonald** started his farming business at age 15, renting a farm to grow crops and stocker cattle. He is now a partner and CFO at Blue Sky Farms, a family-owned, multi-state dairy and farming operation based in Friona, Texas. Blue Sky Farms operations consist of dairy, alfalfa, cotton, and grain farming throughout the panhandle, south plains, and central areas of Texas.

**Lance D. Morris** farms cotton, wheat and milo in Crosby, Dickens and Floyd counties and resides in Crosbyton, Texas. He owns Morris Farms, which is a farming and ranching operation. Mr. Morris is on the board of directors of the Associated Cotton Growers and White River Municipal Water District.

**Gary L. Palousek** is a self-employed farmer raising cotton, milo and corn in Willacy County, Texas, and operates his businesses individually and as a partner of Las Dos Palmas Farms. Mr. Palousek resides and maintains an office in Raymondville, Texas. He is director and secretary-treasurer of the Willacy County Drainage District No. 2 and is committeeman of Willacy County Farm Service Agency.

**Danny Parker** is engaged in row crop farming and a cow/calf operation in Uvalde County and conducts his business as Danny Parker Farms. Mr. Parker resides in Uvalde, Texas, and serves as the executive director of the Gulf Compress in Corpus Christi, Texas, a cotton compress and warehouse business. Mr. Parker is also a member of the Uvalde County Livestock Show Steer.

**Ronnie Riddle** is owner and operator of Riddle Farms, a farming and ranching operation headquartered in Jones County, Texas, near Hamlin. He resides in Abilene, Texas, and farms in Fisher, Stonewall, Jones and Haskell counties. Mr. Riddle is a board member of the Texas Trail Council of the Boy Scouts of America.

**Shane Sklar** is a fourth-generation farmer and rancher from Edna, Texas. He is the owner of El Toro Farms, which specializes in cotton and corn production. He is also an owner in Sklar & Son Cattle, a cow-calf operation with cattle in Jackson and Bee counties. Mr. Sklar is a manager of Sklar Seed, a grain sorghum, soybean and corn seed sales company that markets the LG Seeds brand.

**R. H. "Steve" Stevens** is a certified public accountant, primarily as a consultant to Ham, Langston & Brezina of Houston, Harris County, Texas. Mr. Stevens resides in Houston, Texas, and is a member of the board of partners for ANCO Insurance in Bryan, Texas, member of the board of directors of the Houston Livestock Show and Rodeo and member of the board of directors of the American Quarter Horse Association. Mr. Stevens also has a cattle/horse operation in Burleson County, Texas.

**Sharleen Walkoviak** resides in Houston, Texas, and is a co-owner of Covenant Technology Services LLC, which provides outsourced IT and consulting services and is based in Houston, Harris County, Texas. She is a member of the board of directors of the Houston Livestock Show and Rodeo. Other roles and responsibilities include serving as president of Amigas Para Niños, vice president of Books Between Kids and membership chairman of the Advisory Council of The Bush School of Government and Public Service at Texas A&M.

**Lowell Woodward** ranches in Pecos, Crockett, Brewster and Upton counties, and resides in Pecos County, Texas. Mr. Woodward raises sheep, goats, cattle and horses, and has a hunting operation. He is a director of the Texas Sheep and Goat Raisers Association and owns Woodward Inc., an apartment complex.

**Joe David Yates** resides in Mason, Texas, and ranches in Texas and New Mexico. Mr. Yates sells ranch real estate in Texas, New Mexico and Oklahoma, with an office in Mason, Texas. He is the owner and president of Joe David Yates Inc.; is part owner of Bay City Feeds, a feed operation in Bay City, Texas; is a director on the Farm Credit Council; and is the vice president/secretary of Stewart Ranch with operations in Texas and New Mexico.

**Jeff Norte** serves as the association's president and chief executive officer. Mr. Norte has been with the association since September 2010. Prior to joining the association, he served in various credit and risk positions, including overseeing credit for CoBank's corporate and international portfolio, as well as several years as a regulator in Kansas City with the FDIC. He is a veteran of the military, serving with the U.S. Army. Mr. Norte is a certified public accountant and received his MBA from Concordia University Texas.

**Chris Burt** serves as the association's chief human resources officer. Mr. Burt joined the association in 2021. Prior to joining the association, he served as the executive vice president, chief employee experience officer for GM Financial in Fort Worth, Texas. He is a certified senior professional in human resources (SPHR). Mr. Burt received his undergraduate degree in psychology from Auburn University and his Master of Business Administration from the University of Texas at Arlington.

**Jon Hutchinson** serves as the association's chief credit officer. He joined the association in 2010 as a senior credit officer and has held a variety of credit leadership positions, most recently senior vice president and director of commercial credit. Prior to joining the association, Mr. Hutchinson served in credit leadership positions with John Deere Credit and as an examiner with the Farm Credit Administration. He has a Bachelor of Science in agricultural business from Colorado State University, and a Master of Science in business administration from Iowa State University.

**Sally Lawson** serves as the association's chief financial officer. Mrs. Lawson joined Capital Farm Credit in 2004 and has more than 30 years of financial and accounting experience. She has held various roles in the finance department, most recently as the vice president of finance. Mrs. Lawson has a bachelor's degree in finance from Texas Tech University, and an advanced degree from the American Bankers Association Stonier Graduate School of Banking, in partnership with University of Pennsylvania's Wharton School of Business. In addition, she holds a certificate of leadership from the Wharton School of Business.

**Phil Peabody** serves as the association's chief lending officer. Mr. Peabody has been with association since 2004. He has served in various roles in the association, most recently leading the enterprise risk management function as chief risk officer. Prior to that, he served as a branch manager and loan officer in West Texas. Mr. Peabody has bachelor's and master's degrees in agricultural and applied economics from Texas Tech University.

**Wes Sutton** serves as the association's general counsel and manages the legal department. Mr. Sutton earned his undergraduate degree from Erskine College and his Juris Doctorate from the University of South Carolina School of Law and is a member of the South Carolina Bar and the State Bar of Texas. Prior to his employment with the association, he was general counsel and executive vice president with AgSouth Farm Credit. He has also held several positions in the legal department at AgFirst Credit Bank and has over 20 years of service with the Farm Credit System.

**Jennifer Thompson** serves as the association's chief administrative officer. Ms. Thompson joined Capital Farm Credit in 2013 where she has served within the internal credit review team before managing association efforts around compliance and procedures as senior vice president of compliance. Prior to joining the association, Ms. Thompson was a commissioned examiner with the Farm Credit Administration. Ms. Thompson has a Bachelor of Business Administration in finance from Texas A&M University.

**Glenn Trant** serves as the association's chief operating officer. Mr. Trant joined Capital Farm Credit in 2008 after a merger with First Ag Credit and has more than 30 years of Farm Credit experience. Mr. Trant previously served as interim chief lending officer; senior vice president, lending and relationship management; as well as regional president. He has a Bachelor of Science in agricultural economics and an MBA in finance and accounting from Texas A&M University.

## COMPENSATION OF DIRECTORS AND SENIOR OFFICERS

During 2022, directors were compensated for their service to the association in the form of an honorarium of $1,500 per month, $600 per day for each meeting attended, $200 per meeting for conference calls and $500 for travel days when required. Committee chairperson receives an additional $200 per meeting for committee meetings. The board chairperson and vice chairperson were compensated $800 per meeting for each board meeting attended, and directors were also reimbursed for certain expenses incurred while representing the association in an official capacity. Mileage for attending official meetings during the first half of 2022 was paid at the IRS-approved rate of 58.5 cents per mile and 62.5 cents per mile from July 1, 2022 to December 31, 2022. A copy of the travel policy is available to stockholders of the association upon request.

**Number of Days Served**

| Director | Board Meetings | Other Official Activities | Total Compensation in 2022 |
|---|---|---|---|
| Paul Aelvoet | 9 | 22 | 39,000 |
| Jim Brock | 2 | 5 | 10,200 |
| Kenny Brown | 9 | 21 | 37,700 |
| Dale Crenwelge | 8 | 14 | 35,900 |
| Rachel Cutrer | 3 | 5 | 10,800 |
| Josh Eilers | 9 | 15 | 37,100 |
| Kelly Gaskins | 5 | 8 | 23,500 |
| Dale Hoelscher | 9 | 13 | 33,000 |
| Jerred Hurst | 8 | 13 | 31,600 |
| Kenton B. Kimball | 9 | 41 | 63,400 |
| John Malazzo | 9 | 32 | 51,300 |
| Terry McAlister | 7 | 19 | 33,800 |
| Josh McDonald | 3 | 5 | 12,800 |
| Lance D. Morris | 8 | 12 | 34,400 |
| Gary L. Palousek | 9 | 13 | 35,900 |
| Danny Parker | 9 | 12 | 40,000 |
| Ronnie Riddle | 9 | 10 | 32,600 |
| Shane Sklar | 9 | 13 | 32,900 |
| Steve Stevens | 6 | 9 | 24,100 |
| Sharleen Walkoviak | 9 | 20 | 37,200 |
| Lowell Woodward | 9 | 13 | 36,400 |
| Joe David Yates | 6 | 14 | 25,000 |
| | | | $ 718,600 |

There were seven board meetings during 2022. The aggregate compensation paid to directors in 2022, 2021 and 2020 was $718,600, $646,500 and $706,400, respectively.

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

| | Committee | | | | |
|---|---|---|---|---|---|
| **Director** | **Audit** | **Compensation** | **Governance** | **Other*** | **Total** |
| Paul Aelvoet | $ - | $ - | $ 5,400 | $ 9,200 | $ 14,600 |
| Jim Brock | 1,200 | - | - | 1,800 | 3,000 |
| Kenny Brown | - | - | 4,200 | 8,600 | 12,800 |
| Dale Crenwelge | 3,000 | - | 200 | 5,400 | 8,600 |
| Rachel Cutrer | - | - | 1,200 | 1,800 | 3,000 |
| Josh Eilers | - | - | 3,800 | 5,400 | 9,200 |
| Kelly Gaskins | - | 1,200 | - | 3,800 | 5,000 |
| Dale Hoelscher | 600 | 4,800 | 600 | 3,600 | 9,600 |
| Jerred Hurst | - | - | 3,600 | 4,200 | 7,800 |
| Kenton Kimball | 3,000 | 3,600 | 3,000 | 15,600 | 25,200 |
| John Malazzo | 3,000 | 3,600 | 3,600 | 10,400 | 20,600 |
| Terry McAlister | 2,400 | - | 200 | 9,000 | 11,600 |
| Josh McDonald | - | - | 1,200 | 1,800 | 3,000 |
| Lance Morris | - | 3,000 | 200 | 4,400 | 7,600 |
| Gary Palousek | - | 3,600 | - | 4,400 | 8,000 |
| Danny Parker | - | 3,000 | 200 | 4,400 | 7,600 |
| Ronnie Riddle | 1,200 | - | 2,600 | 2,400 | 6,200 |
| Shane Sklar | - | - | 3,800 | 4,200 | 8,000 |
| Steve Stevens | 2,400 | - | - | 3,600 | 6,000 |
| Sharleen Walkoviak | 3,400 | - | 600 | 8,800 | 12,800 |
| Lowell Woodward | - | 3,600 | - | 4,400 | 8,000 |
| Joe David Yates | 1,800 | - | 600 | 6,000 | 8,400 |
| | $ 22,000 | $ 26,400 | $ 35,000 | $ 123,200 | $ 206,600 |

*Other includes the following meetings that were held: credit, compensation training, director development, national director conference, new director orientation, Texas District Conference, Director Advancement Program (DAP), Director Leadership, Risk, Farm Credit Council and FCBT stockholder, Risk 360, compliance and audit conference.

The aggregate amount of reimbursement for travel, subsistence and other related expenses paid to directors and on their behalf was $376,503, $252,623 and $155,138, in 2022, 2021 and 2020, respectively.

## COMPENSATION OF SENIOR OFFICERS

### Compensation Discussion and Analysis – Senior Officers

A critical factor to the association's success is its ability to attract, develop and retain staff who are knowledgeable and efficient in their ability to support the association in the execution of its strategic objectives and delivery of association results that maximize the value received by its membership. The association operates utilizing a compensation program that focuses on the performance and contributions of its employees in achieving the association's financial and operational objectives, all for the ultimate benefit of its membership. The association's board of directors, based on recommendations of its Compensation Committee, establishes the salary and approves the incentive programs utilizing data derived from independent third-party compensation specialists in the financial services sector to ensure incentive structures are in line with market-comparable positions. Studies provided by third-party compensation specialists form the foundation for evaluation and establishment of salary and incentive plans used by the association.

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

CEO Compensation

| Name of Individual | Year | Salary (a) | Long-Term Incentives (b) | Current Year Incentives (c) | Other (d) | Change in Pension Value (e) | Total* |
|---|---|---|---|---|---|---|---|
| Jeff Norte, CEO | **2022** | **$ 578,256** | **$ 83,115** | **$ 254,350** | **$ 53,755** | **$ -** | **$ 969,476** |
| Jeff Norte, CEO | 2021 | 487,534 | 95,653 | 145,489 | 29,697 | - | 758,373 |
| Ben R. Novosad, CEO | 2021 | 633,359 | 374,838 | 471,028 | 268,175 | | 1,747,400 |
| Ben R. Novosad, CEO | 2020 | 913,481 | 249,665 | 320,942 | 58,947 | 580,392 | 2,123,427 |

(a) Gross salary
(b) Cash payout of long-term incentives
(c) Cash payout of annual incentives
(d) Includes contributions to 401(k) and defined contribution plans, automobile benefits that may exceed $5,000 and premiums paid for life insurance
(e) Change in pension value represents the change in the actuarial present value of the accumulated benefit under the defined benefit pension plan, the Farm Credit Bank of Texas Pension Plan, from the prior fiscal year to the current fiscal year.

Refer to Note 13 – Employee Benefit Plans for detailed explanation on the increase to the retiree welfare plan's projected benefit obligation and corresponding impact to change in pension value.

*The table above does not include the estimated long-term incentive accruals of $939,621. For details regarding these accruals, see disclosure more fully discussed within the LTI section of this discussion and analysis.

Pension Benefits

During 2021, the previous CEO, Ben Novosad, retired from the association and there is no pension benefit information to report for 2021.

Compensation of Other Senior Officers

The following table summarizes the compensation paid to all senior officers, excluding the CEO, of the association during 2022, 2021 and 2020. Amounts reflected in the table are presented in the year the compensation was paid.

| Name of Group | Year | Salary (a) | Long-Term Incentives (b) | Current Year Incentives (c) | Other (d) | Change in Pension Value (e) | Total* |
|---|---|---|---|---|---|---|---|
| Aggregate No. of Senior Officers in Year Excluding CEO | | | | | | | |
| **7** | **2022** | **$ 1,953,247** | **$ 190,712** | **$ 688,027** | **$ 258,422** | **$ -** | **$ 3,090,408** |
| 6 | 2021 | 1,476,733 | 99,969 | 450,386 | 248,363 | - | 2,275,451 |
| 6 | 2020 | 1,910,627 | 339,533 | 669,252 | 324,611 | 1,654,786 | 4,898,809 |

(a) Gross salary
(b) Cash payout of long-term incentives
(c) Cash payout of annual incentives
(d) Includes contributions to 401(k) and defined contribution plans, automobile benefits that may exceed $5,000 and premiums paid for life insurance.
(e) Change in pension value represents the change in the actuarial present value of the accumulated benefit under the defined benefit pension plan, the Farm Credit Bank of Texas Pension Plan, from the prior fiscal year to the current fiscal year.

Refer to Note 13 – Employee Benefit Plans for detailed explanation on the increase to the retiree welfare plan's projected benefit obligation and corresponding impact to change in pension value.

*The table above does not include the estimated LTI incentive accruals of $1,557,714. For details regarding these accruals, see disclosure more fully discussed within the long-term incentives section of this discussion and analysis.

Disclosure of total compensation paid to any senior officer included in the summary compensation table above is available to our shareholders upon request.

Pension Benefits

During 2021, the previous senior officer who was a participant in the Farm Credit Bank of Texas Pension Plan retired from the association. No other officer included in the table above participates in the plan. Disclosure of information on the total compensation paid and the arrangements of the compensation plans during the last fiscal year to any senior officer or to any other officer included in the aggregate are available and will be disclosed to shareholders of the association upon request.

Additional Nonqualified Supplemental 401(k) Plan:

During 2022, the association continued to plan for succession for key members of senior management who are reaching retirement eligibility. In conjunction with this plan during 2018, the association entered into an agreement with one of its senior management team members that called for a one-time discretionary contribution into the Farm Credit Benefits Alliance Nonqualified Supplemental 401(k) Plan ("the Plan"). The association evaluated the need to restore a portion of benefits lost as a result of the addition of a member to the association's senior management team, and as a result developed a plan to address this shortfall and funded this plan during 2018. Expenses of the plan relating to this agreement for 2022, 2019 and 2020 were $0, $0 and $0 respectively.

Incentive Plan for Officers and Employees:

The association utilizes two incentive plans: the annual (short-term) incentive plan (STI) based on individual and association performance that drives behavior that supports annual association goals, and the Long-Term Incentive plan (LTI), which was developed to reward key employees for achievement of the association's long-term goals and objectives. Both plans utilize parameters for measuring achievement at either threshold, target or superior performance levels. The LTI evaluates performance annually and is earned over a rolling three-year performance period.

Annual (Short-Term) Incentive Plan (STI)

The STI plan is a balanced scorecard plan that rewards employees for achieving desired business goal objectives for the year. The STI is an annual plan that is administered by the board.

At the beginning of each plan year, the board reviews and approves STI plan performance objectives for the association and the award matrix by which all incentives under the STI shall be calculated. Each STI plan participant is assigned an incentive award target calculated as a percentage of base pay that may be awarded if the association and participant achieve target performance goals. Failure to meet minimum thresholds for individual goals will result in no incentive, while achievement at superior levels for individual goals will result in the maximum incentive opportunity available at that salary grade for that goal. Potential individual award percentages vary based upon an employee's job grade level and are higher for those persons serving to direct performance of the association, which includes its senior lending staff and senior officers. Award payments vary depending upon the extent to which the association goals are achieved.

For calendar year 2022, the board approved the following goal performance measures, weightings and performance goals:

| Performance Measures | Weight | Performance Goals Target | 2022 Actual Performance | Performance Achievement |
|---|---|---|---|---|
| Acceptable credit quality as percentage of total loans | 20% | 96.00% | 98.37% | Superior |
| Net charge-offs as percentage of average loans plus other property owned | 10% | 0.10% | 0.00% | Superior |
| Nonearning assets as percentage of loans plus other property owned | 10% | 0.60% | 0.53% | Between Target & Superior |
| Return on equity results compared to System peer group | 40% | 3rd of System peers | 1st | Superior |
| Loan Growth - Net change in 12 Month Avg of Managed Volume (recorded investment + participations sold plus syndicated loans agented for CFC Customers) | 20% | 8% | 17.63% | Superior |
| Total | 100% | | | |

As part of this plan, the association has also established parameters for goal performance that define threshold and superior levels of incentive opportunities when more or less than the targeted goals are achieved. If less than the threshold level of performance is achieved for a particular performance measure, no incentives will be awarded for that performance measure. Financial results for 2022 resulted in the association's achievement of goal performance that overall achieves superior goals in four of the five measures. As a result, the board approved, and the association accrued an estimated payment of $17,221,548 in STI incentives. As specified by the plan, these incentives are to be paid by March 15, 2023.

Long-Term Incentive Plan (LTI)

The purpose of the association's LTI is to offer a financial rewards package to key employees based on the long-term performance of the association. The board is the administrator of the LTI. The board has retained the authority to review and approve plan participants, the incentives prior to payment and the LTI metrics and goals as presented by the CEO and members of management. Any additions or deletions to the participant list must be submitted for board approval prior to the beginning of a performance period (the consecutive 36-month period beginning January 1 and ending December 31). Each participant is assigned an incentive award goal, calculated as a percentage of base salary at the beginning of the performance period at threshold, target and superior performance levels.

At the beginning of each calendar year, the board approves the LTI plan objectives for the association and the award formula or matrix by which all awards under this plan are based. Since its inception in 2011, the LTI plan established goals and metrics that management and the board felt were long term in nature and fostered the long-term health and viability of the association and its stockholders. These goals included loan volume growth, operating efficiency and capital distributions to the association's stockholders. The association's vision is to be the partner of choice for lending and related services in rural America through outstanding people, performance and member value. The board believes the goals established for the LTI support this vision.

For the LTI performance period 2022-2024, the board approved the following goal performance measures, weightings and performance goals, which are consistent with goals established for the LTI plan performance periods of 2020-2022 and 2021-2023.

| | Performance Goals | |
|---|---|---|
| **Performance Measures** | **Target** | **Weight** |
| Capital distributions- Three-year average annual cash patronage plus allocated equity retirements in excess of certain % of average accrual loans | 1.0% | 33.3% |
| Loan Growth - Three Year Avg of Net Change in 12 Month Avg of Managed Volume (Recorded Investments + Participations Sold + Syndicated Loans Agented for CFC Customers) | 8.0% | 33.3% |
| Three-year average operating expenses as a percentage of net interest income plus other income | 3rd of large system associations | 33.4% |

The actual/projected results for LTI performance and the estimated incentives based upon the performance for each of the three performance periods are as follows:

| | Performance Level | | | | | |
|---|---|---|---|---|---|---|
| **Plan Period** | **Capital Distributions** | **Growth** | **Efficiency** | **CEO LTI** | **Senior Officer LTI** | **Other Officers LTI** |
| 2020-2022 projected | superior | between threshold & target | between target & superior | $ 235,521 | $ 490,401 | $ 495,738 |
| 2021-2023 projected | superior | between target & superior | between target & superior | 104,078 | 591,511 | 626,374 |
| 2022-2024 projected | superior | superior | superior | 385,000 | 839,216 | 1,222,683 |

Other

Employees who use their personal automobile for business purposes were reimbursed during 2022 at the IRS-approved rate of 58.5 cents per mile from January 1, 2022 to June 30, 2022, and 62.5 cents per mile from July 1, 2022 to December 31, 2022.

Senior officers, including the CEO, are reimbursed for reasonable travel, subsistence and other related expenses while conducting association business. Neither the CEO nor any other senior officer received noncash compensation exceeding $5,000 in 2022, 2021 or 2020. A copy of the association's travel policy is available to shareholders upon request.

## TRANSACTIONS WITH DIRECTORS AND SENIOR OFFICERS

The association's policies on loans to and transactions with its officers and directors, required to be disclosed in this section, are incorporated herein by reference from Note 14 to the consolidated financial statements, "Related Party Transactions," included in this annual report.

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

During the past five years, none of the association's officers or directors have been involved in legal proceedings that are material to an evaluation of the ability or integrity of any person who served as director or senior officer at any time during the year just ended.

## RELATIONSHIP WITH INDEPENDENT AUDITORS

No change in auditors has taken place since the last annual report to stockholders, and no disagreements with auditors has occurred that the association is required to report to the Farm Credit Administration under part 621 of the FCA regulations governing this disclosure.

Fees for professional services paid by the association during 2022 to PricewaterhouseCoopers are as follows:

| Service Category | Fees |
|---|---|
| Audit-related services | $ 140,616 |
| Nonaudit services* | 16,700 |
| | $ 157,316 |

*Nonaudit services include fees related to the financial statement disclosure checklist and tax compliance services, which were approved by the association's audit committee.

Fees paid in 2022 related to 2021 audit services were $12,555.
Fees paid in 2022 for professional services rendered in 2022 were $128,061.

## RELATIONSHIP WITH UNINCORPORATED BUSINESS ENTITIES

The association and the bank made investments in a limited partnership, the Advantage Capital Ag Partners LP., that will provide junior capital to rural and agriculture businesses in the United States. This partnership is a Rural Business Investment Company (RBIC), and the investment by the association and the bank is allowed under the Mission-Related Investment authorities granted in the Farm Credit Act. The association's investment in RBIC was $13,024, $12,225 and $11,384 at December 31, 2022, 2021 and 2020, respectively. This investment is included on the Consolidated Balance Sheet.

## FINANCIAL STATEMENTS

The financial statements, together with the report thereon of PricewaterhouseCoopers dated March 9, 2023, and the report of management in this annual report to stockholders, are incorporated herein by reference.

## MEMBER/SHAREHOLDER PRIVACY

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

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

The association has a policy to make a concerted effort to finance young, beginning or small farmers and ranchers, and producers or harvesters of aquatic products (YBS program). For purposes of the association's YBS program, young producers are defined as those age 35 or younger. Beginning producers are defined as producers with 10 years or less of experience at farming, ranching or producing or harvesting aquatic products. A small producer is defined as one who normally generates less than $250,000 in annual gross sales of agricultural or aquatic products. Using statistics obtained from a United States Department of Agriculture 2017 census and information from the association's loan accounting records as of December 31, 2022, the following table compares the percentage of YBS farmers in the association's territory (based on USDA data) with the percentage of YBS customers in the association's loan portfolio. Though the measurement (farmers) used in the USDA census information is not directly comparable to the measurement (customers) used by the association, the statistics presented herein serve as a quantitative measurement of the association's success in attracting and making loans to young, beginning and/or small farmers who live or have operations in the association's territory.

In the following table, 4.7 percent of the farmers in the association's territory are "Young" farmers while, 18.1 percent of our customers who live or operate in the association's territory meet the "Young" criterion. The same explanation applies to the Beginning and Small categories.

| FARMERS, RANCHERS, AND PRODUCERS OR HARVESTERS OF AQUATIC PRODUCTS CLASSIFIED AS: | FARMERS IN TERRITORY | ASSOCIATION CUSTOMERS |
|---|---|---|
| Young | 4.7% | 18.1% |
| Beginning | 28.1% | 70.1% |

In the following table, 95.5 percent of the farms in the association's territory are "Small" farms, while 90.3 percent of our customers who live or operate in the association's territory are producers who normally generate less than $250,000 in annual gross sales of agricultural or aquatic products.

| FARMERS, RANCHERS, AND PRODUCERS OR HARVESTERS OF AQUATIC PRODUCTS CLASSIFIED AS: | FARMS IN TERRITORY | ASSOCIATION CUSTOMERS |
|---|---|---|
| Small | 95.5% | 90.3% |

At December 31, 2022, the association had the following number of loans and volume outstanding in its YBS Program (loans may fit in one, two or all three categories):

| YOUNG | | BEGINNING | | SMALL | |
|---|---|---|---|---|---|
| Number of Loans | Volume | Number of Loans | Volume | Number of Loans | Volume |
| 5,230 | $1,322,625 | 18,848 | $5,973,542 | 24,153 | $7,243,696 |

The association maintains a policy that directs management to implement a program that strives to fully utilize its resources to: (A) attract and retain YBS customers; (B) implement lending programs and/or services that meet the needs of YBS customers; and (C) develop quantitative standards that may be used to measure the number of YBS customers served as compared to the number in the CFC territory. Management has implemented programs to address each component by:

Attracting and retaining YBS customers – The employees of Capital Farm Credit are involved in working with youth livestock programs that have historically produced individuals who become farmers and ranchers in the future. Hundreds of hours are spent annually serving in various capacities that promote livestock shows and sales for youth across the state, and Capital Farm Credit spends thousands of dollars sponsoring and contributing to these programs. These programs are spread across the state and include county, regional and statewide shows and involve both 4-H and FFA programs.

In addition, CFC sponsors and supports programs and organizations around the state that are targeted at young, beginning or small farmers or ranchers, some in cooperation with various county and statewide organizations but also with the Texas A&M AgriLife Extension Service. Programs such as the "Next Generation Program" and others have been successful in helping to educate and provide knowledge and other resources to thousands of individuals who are taking steps to initiate or increase their involvement in agriculture or increase the size and productivity of their existing operations. The association is concerned about the next generation of agriculture and utilizes its programs and personnel to help develop those who will be producing food and fiber after the current generation of farmers and ranchers retire.

The involvement and support of these programs also helps YBS farmers/ranchers become aware of Capital Farm Credit and understand how its loan programs and services can be of value to them as they improve or expand their current operations but also aids them in improving or expanding their operation regardless of whether they do business with Capital Farm Credit.

Implementing lending programs and/or services that meet the needs of YBS customers – The association implemented a policy that permits the association to provide constructive credit to serve any financing need of YBS customers who are taking demonstrated steps to become more fully engaged as a full-time farmer or rancher. Also, the association has adopted underwriting standards that contain flexible criteria that permit the credit needs of customers to be met when the customer falls short of meeting an established standard but has one or more compensating strengths to offset the area of weakness. These flexible criteria, while still requiring reasonable and prudent underwriting standards, allow customers who engage in agriculture operations less than full time to have the capital resources they need to begin or grow their operations. In addition, the association cooperates with government agencies to structure loans with third party guarantees when the applicant does not have sufficient equity or proven repayment sources to qualify for credit by themselves. These cooperative efforts allow YBS customers to begin an agriculture operation, maintain their operation through stressful periods or make expansions in herd size, facilities or acreage.

Developing quantitative standards that may be used to measure the number of YBS customers served as compared with the number in the CFC territory – In each year's business plan, the board establishes YBS goals and develops quantitative standards to measure the level of success in achieving the established goals. The business plan also defines how and when the standards will be measured and assigns responsibility to an officer for monitoring, tracking and reporting the standards. The progress in achieving the goals is reported to the board of directors each quarter. Through this process, the board is able to evaluate if the programs implemented by management are successful in achieving the goals in the business plan and are successful in achieving compliance with the board's policy direction to serve the needs of YBS customers.

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