LONE STAR, ACA

2018
Quarterly Report

For the Quarter Ended September 30, 2018

REPORT OF MANAGEMENT

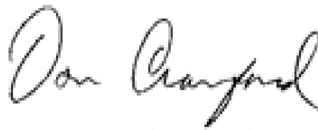
The undersigned certify that we have reviewed this report, that it has been prepared in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate and complete to the best of our knowledge and belief.

William 'Bill' Melton, Interim Chief Executive Officer

November 9, 2018

Amy Birt, Chief Financial Officer

November 9, 2018



Don Crawford, Chairman,
Audit Committee

November 9, 2018

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion and analysis reviews the consolidated financial performance of Lone Star, ACA ("ACA") including its wholly owned subsidiaries Lone Star Ag Credit, FLCA and Lone Star Ag Credit, PCA (collectively referred to herein as the "Association") for the quarter ended September 30, 2018. The discussion should be read in conjunction with the Association's Annual Report to Stockholders, and notes thereto, for the year ended December 31, 2017. Operating results for the nine months ended September 30, 2018 are not necessarily indicative of the results for the year ending December 31, 2018 or any future period.

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

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The consolidated financial statements were prepared under the oversight of the Association's Audit Committee.

Patronage:

In July 2018, the Association's board of directors approved to pay a cash patronage, which was paid in September of 2018, based on 2017 earnings. The patronage was paid to eligible borrowers based on their average outstanding loan balance for the year ending December 31, 2017. The patronage amount paid was $7,049,955.

In 2017, the Association paid cash patronage of $13,809,745, based on 2016 earnings. Patronage was paid to eligible borrowers based on their average outstanding loan balance for the year ended December 31, 2016.

In December 2017, the Association received a direct loan patronage of $5,355,288 from the Farm Credit Bank of Texas ("Bank"), representing 39 basis points on the average daily balance of the Association's direct loan with the Bank. During 2017, the Association received $571,987 in patronage payments from the Bank, based on the Association's stock investment in the Bank. Additionally, the Association received a participation's patronage of $18,615 in 2017 from the Bank, representing 75 basis points on the Association's average balance of participations sold into the Bank's patronage pool program.

Loan Portfolio:

Total loans outstanding at September 30, 2018, including nonaccrual loans and sales contracts, were $1,603,354,136 compared to $1,681,072,602 at December 31, 2017, reflecting a decrease of 4.6 percent. Nonaccrual loans as a percentage of total loans outstanding were 0.3 percent at September 30, 2018, compared to 0.3 percent at December 31, 2017.

Total loans outstanding at September 30, 2017, including nonaccrual loans and sales contracts, were $1,701,198,640. Nonaccrual loans as a percentage of total loans outstanding were 0.4 percent at September 30, 2017.

The Association recorded $277,548 in recoveries and $124,270 in charge-offs for the quarter ended September 30, 2018, and $211,591 in recoveries and $332,791 in charge-offs for the same period in 2017. The Association's allowance for loan losses was 0.6 percent, 0.5 percent and 0.7 percent of total loans outstanding as of September 30, 2018, December 31, 2017 and September 30, 2017, respectively.

Since 1917, the Association and its predecessors have provided its members with quality financial services. The board of directors and management remain committed to maintaining the financial integrity of the Association while offering competitive loan products that meet the financial needs of agricultural producers.

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. The following table illustrates the Association's components and trends of high-risk assets.

	September 30, 2018		December 31, 2017		September 30, 2017	
	Amount	**%**	Amount	%	Amount	%
Nonaccrual	**$ 4,667,808**	**74.8%**	$ 5,633,106	55.4%	$ 6,134,054	57.8%
90 days past due and still accruing interest	**-**	**0.0%**	-	0.0%	1,366,656	12.9%
Formally restructured	**1,570,593**	**25.2%**	4,537,338	44.6%	3,103,044	29.3%
Total	**$ 6,238,401**	**100.0%**	$ 10,170,444	100.0%	$ 10,603,754	100.0%

Results of Operations:

The Association had net income of $4,451,448 and $23,216,564 for the three and nine months ended September 30, 2018, as compared to net loss of $1,805,618 and net income of $4,207,660 for the same period in 2017, reflecting an increase of 346.5 and 451.8 percent. Net interest income was $11,061,253 and $37,118,015 for the three and nine months ended September 30, 2018, compared to $11,614,790 and $35,182,071 for the same period in 2017.

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	Nine months ended			
	September 30, 2018		September 30, 2017	
	Average Balance	**Interest**	Average Balance	Interest
Loans	**$ 1,654,261,505**	**$ 63,616,695**	$ 1,683,262,450	$ 58,184,030
Total interest-earning assets	**1,654,261,505**	**63,616,695**	1,683,262,450	58,184,030
Interest-bearing liabilities	**1,326,816,488**	**26,498,680**	1,366,752,572	23,001,959
Impact of capital	**$ 327,445,017**		$ 316,509,878	
Net interest income		**$ 37,118,015**		$ 35,182,071

	2018 Average Yield	2017 Average Yield
Yield on loans	**5.14%**	4.62%
Total yield on interest-earning assets	**5.14%**	4.62%
Cost of interest-bearing liabilities	**2.67%**	2.25%
Interest rate spread	**2.47%**	2.37%
Net interest income as a percentage of average earning assets	**3.00%**	2.79%

	Three months ended September 30, 2018 vs. September 30, 2017		
	Increase (decrease) due to		
	Volume	**Rate**	**Total**
Interest income - loans	**$ (1,002,455)**	**$ 6,435,120**	**$ 5,432,665**
Total interest income	**(1,002,455)**	**6,435,120**	**5,432,665**
Interest expense	**(672,105)**	**4,168,826**	**3,496,721**
Net interest income	**$ (330,350)**	**$ 2,266,294**	**$ 1,935,944**

Interest income for the three and nine months ended September 30, 2018, increased by $336,141 and $5,432,665, or 1.7 and 9.3 percent respectively, from the same period of 2017, primarily due to increases in yields on earning assets, fair value accretion recognition, and foregone interest recoveries; offset by a decrease in average loan volume. Interest expense for the three and nine months ended September 30, 2018, increased by $889,678 and $3,496,721, or 10.9 and 15.2 percent, from the same period of 2017 due to an increase in cost of funds; offset by a decrease in average debt volume. Average loan volume for the third quarter of 2018 was $1,622,757,394, compared to $1,694,019,424 in the third quarter of 2017. The average net interest rate spread on the loan portfolio for the third quarter of 2018 was 2.13 percent, compared to 2.29 percent in the third quarter of 2017.

The Association's return on average assets for the nine months ended September 30, 2018, was 1.83 percent compared to 0.33 percent for the same period in 2017. The Association's return on average equity for the nine months ended September 30, 2018, was 8.82 percent, compared to 1.68 percent for the same period in 2017.

Interest income was affected by the accretion of the fair value of loan concessions recorded in response to the breach of Association policies and procedures by a former loan officer as more fully described in the Association's 2017 Annual Report. Accretion of the concessions increased interest income for the nine months ended September 30, 2018 and 2017 by $ 718,182 and $ 92,503 , respectively. The increased accretion for the nine months ended September 30, 2018 compared to the same period in 2017 reflects the acceleration of accretion due to early pay-off of three loans with concessions.

Noninterest income for the three and nine months ended September 30, 2018, increased by $241,376 and $1,248,813, or 14.0 and 23.5 percent, respectively, compared to the same period of 2017, primarily due to increases in other noninterest income which includes $963,257 of excess insurance funds balances in the allocated insurance reserve accounts (AIRCs) from the Farm Credit System Insurance Corporation (FCSIC). Noninterest expenses for the three and nine months ended September 30, 2018, decreased by $5,527,875 and $12,916,450, or 42.3 and 38.5 percent, respectively, compared to the same period of 2017, due mostly to expenses related to the breach of Association policies and procedures by a former loan officer in 2017 as more fully described in our 2017 Annual Report with no comparable expense in 2018. Provisions for loan losses for the three and nine months ended September 30, 2018, decreased by $1,021,493 and $2,847,491, or 49.2 and 103.7 percent, respectively, compared to the same period of 2017 primarily due to the resolution of uncertainties with respect to loans involved in the breach of Association policies and procedures by a former loan officer in 2016 and 2017.

Liquidity and Funding Sources:

The Association secures the majority of its lendable funds from the Bank, which obtains its funds through the issuance of System-wide obligations, and with lendable equity. The following schedule summarizes the Association's borrowings.

	September 30, 2018	December 31, 2017	September 30, 2017
Note payable to the Bank	**$ 1,271,643,908**	$ 1,358,683,640	$ 1,389,365,902
Accrued interest on note payable	**2,891,107**	2,807,131	2,647,574
Total	**$ 1,274,535,015**	$ 1,361,490,771	$ 1,392,013,476

The Association operates under a general financing agreement (GFA) with the Bank. The current GFA is effective through September 30, 2020. The primary source of liquidity and funding for the Association is a direct loan from the Bank. The outstanding balance of $1,271,643,908 as of September 30, 2018, is recorded as a liability on the Association's balance sheet. The note carried a weighted average interest rate of 2.79 percent at September 30, 2018. The indebtedness is collateralized by a pledge of substantially all of the Association's assets to the Bank and is governed by the GFA. The decrease in note payable to the Bank and related increase in accrued interest payable since December 31, 2017, correlates directly with the overall decrease in Association accrual loan volume and increased cost of funds for the period. The Association's own funds, which represent the amount of the Association's loan portfolio funded by the Association's equity, were $ 331,519,298 at September 30, 2018. The maximum amount the Association may borrow from the Bank as of September 30, 2018, was $ 1,539,840,388 as defined by the GFA. The indebtedness continues in effect until the expiration date of the GFA, which is September 30, 2020, 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.

On August 28, 2017 the Association received a "Notice of Default of General Financing Agreement" from the Bank. The default was due to the Association's nonperformance as it relates to financial reporting. Additionally, the Association was subject to development of action plans for remediation of the Association's material weaknesses noted in the Report on Internal Controls over Financial Reporting. The Association was granted a Waiver of Default of the GFA. The Bank granted the waiver with conditions that the restated financials for fiscal years 2016 and 2017 were provided no later than May 31, 2018. The Association was able to meet the documented requirements of the Waiver.

During the preparation of the 2017 and restated 2016 financial statements, the Association became aware of a financial performance covenant violation of its GFA with the Bank. Specifically, the ROA was revealed to fall below the 1.0% required level. The Association sought and received a temporary waiver of this violation. As of September 30, 2018 the Association is in compliance with this GFA covenant.

Capital Resources:

The Association's capital position increased by $15,806,565 at September 30, 2018, compared to December 31, 2017 and by $22,622,487 compared to September 30, 2017. The Association's debt as a percentage of members' equity was 3.61:1 as of September 30, 2018, compared to 4.03:1 as of December 31, 2017 and 4.20:1 as of September 30, 2017.

Farm Credit Administration regulations require us to maintain minimums for various regulatory capital ratios. New regulations became effective January 1, 2017, which replaced the previously required core surplus and total surplus ratios with common equity tier 1, tier 1 capital, and total capital risk-based capital ratios. The new regulations also added tier 1 leverage and unallocated retained earnings and equivalents (UREE) ratios. The permanent capital ratio continues to remain in effect, with some modifications to align with the new regulations. As of September 30, 2018, the Association exceeded all regulatory capital requirements.

Significant Recent Accounting Pronouncements:

In August 2018, the Financial Accounting Standards Board (FASB) issued guidance entitled "Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Cost." The guidance aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software license). The accounting for the service element of a hosting arrangement that is a service contract is not affected by this guidance. This guidance becomes effective for interim and annual periods beginning after December 15, 2019. The guidance also requires an entity (customer) to expense the capitalized implementation costs of a hosting arrangement that is a service contract over the term of the hosting arrangement. It further specifies where to present expense and payments in the financial statements. Early adoption is permitted. The guidance is to be applied on a retrospective or prospective basis to all implementation costs incurred after the date of adoption. The Association is evaluating the impact of adoption on the Association's financial condition and its results of operations.

In August 2018, the FASB issued guidance entitled "Disclosure Framework — Changes to the Disclosure Requirements for Defined Benefit Plans." The guidance modifies the disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. This guidance becomes effective for fiscal years ending after December 15, 2020. Early adoption is permitted. The guidance is to be applied on a retrospective basis for all periods. The adoption of this guidance will not impact the Association's financial condition or its results of operations, but will impact the employee benefit plan disclosures.

In August 2018, the FASB issued guidance entitled "Disclosure Framework — Changes to the Disclosure Requirements for Fair Value Measurement." The guidance modifies the requirements on fair value measurements by removing, modifying or adding to the disclosures. This guidance becomes effective for interim and annual periods beginning after December 15, 2019. Early adoption is permitted and an entity is permitted to early adopt any removal or modified disclosures and delay adoption of the additional disclosures until their effective date. The adoption of this guidance will not impact the Association's financial condition or its results of operations, but will impact the fair value measurements disclosures.

In February 2018, the FASB issued guidance entitled "Income Statement — Reporting Comprehensive Income — Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income." This guidance allows for the reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the recently issued tax legislation, Tax Cuts and Jobs Act (TCJA) that lowered the federal corporate tax rate from 35% to 21%. The amount of the reclassification shall include the effect of the change in the tax rate on gross deferred tax amounts and related valuation allowances at the date of enactment of the TCJA related to items remaining in accumulated other comprehensive income. The guidance becomes effective for financial statements issued for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. The Association is evaluating the impact of adoption on the Association's financial condition and its results of operations.

In August 2017, the FASB issued guidance entitled "Targeted Improvements to Accounting for Hedging Activities." The guidance better aligns an entity's risk management activities and financial reporting for hedging relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. The amendments in this guidance require an entity to present the earnings effect of the hedging instrument in the same income statement line item in which the earnings effect of the hedged item is reported. This guidance also addresses the timing of effectiveness testing, qualitative and quantitative effectiveness testing and components that can be excluded from effectiveness testing. This guidance becomes effective for interim and annual periods beginning after December 15, 2018. The Association is evaluating the impact of adoption on the Association's financial condition and its results of operations.

In March 2017, the FASB issued guidance entitled "Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Cost." The guidance requires that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. Other components are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. This guidance became effective for interim and annual periods beginning after December 15, 2017. The adoption

of this guidance did not materially impact the Association's financial condition but did change the classification of certain items in the results of operations.

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

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

In February 2016, the FASB issued guidance entitled "Leases." The guidance requires the recognition by lessees of lease assets and lease liabilities on the balance sheet for the rights and obligations created by those leases. Leases with lease terms of more than 12 months are impacted by this guidance. In July 2018, the FASB issued an update entitled "Leases – Targeted Improvements," which provides entities with an additional (and optional) transition method to adopt the new leases standard. Under this new transition method, an entity initially applies the new leases standard at the adoption date and recognizes a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. An entity that elects this additional transition method must provide the required disclosures of the now current standard for all prior periods presented. The guidance and related amendments in this update become effective for interim and annual periods beginning after December 15, 2018, with early application permitted. The Association is evaluating the impact of adoption on its financial condition and results of operations.

In January 2016, the FASB issued guidance entitled "Recognition and Measurement of Financial Assets and Liabilities." The guidance affects, among other things, the presentation and disclosure requirements for financial instruments. For public entities, the guidance eliminates the requirement to disclose the methods and significant assumptions used to estimate the fair value of financial instruments carried at amortized cost. This guidance becomes effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance did not impact the Association's financial condition or its results of operations but did impact the Association's fair value disclosures.

In May 2014, the FASB issued guidance entitled, "Revenue from Contracts with Customers." The guidance governs revenue recognition from contracts with customers and requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Financial instruments and other contractual rights within the scope of other guidance issued by the FASB are excluded from the scope of this new revenue recognition guidance. The guidance sets forth the requirement for new and enhanced disclosures. The Association adopted the new standard effective January 1, 2018, using the modified retrospective approach. As the majority of the Association's revenues are not subject to the new guidance, the adoption of the guidance did not have a material impact on the financial position, results of operations, equity or cash flows.

Regulatory Matters:

The Association is currently operating under a Special Supervision letter issued by the FCA. Lone Star is cooperating and complying with the requirements of the Special Supervision letter and has not been assessed any monetary penalties by the FCA. However, there can be no assurances that future monetary penalties that would affect our financial condition will not be assessed by the FCA.

On March 10, 2016, the Farm Credit Administration approved a final rule to modify the regulatory capital requirements for System Banks and Association's. The stated objectives of the proposed rule are as follows:

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

The Association implemented the new regulatory capital ratios effective on January 1, 2017. The Association's regulatory ratios remained well above regulatory minimums, including the conservation and leverage buffers as of September 30, 2018 and December 31, 2017.

Relationship with the Farm Credit Bank of Texas:

The Association's financial condition may be impacted by factors that affect the Bank. The financial condition and results of operations of the Bank may materially affect the stockholder's investment in the Association. The Management's Discussion and Analysis and Notes to Financial Statements contained in the 2017 Annual Report of the Association more fully describe the Association's relationship with the Bank.

The Texas Farm Credit District's ("District") annual and quarterly stockholder reports, as well as those of the Bank, are available free of charge, upon request. These reports can be obtained by writing to Farm Credit Bank of Texas, The Ag Agency, P.O. Box 202590, Austin, Texas 78720, or by calling (512) 483-9204. Copies of the district's quarterly and annual stockholder reports also can be requested by e-mail at *fcb@farmcreditbank.com*. The annual and quarterly stockholder reports for the Bank and the district are also available on its website at *www.farmcreditbank.com.*

The Association's quarterly stockholder reports are also available free of charge, upon request. These reports can be obtained by writing to Lone Star, ACA, 1612 Summit Avenue, Suite 300, Fort Worth, Texas 76102 or calling (817) 332-6565. The annual and quarterly stockholder reports for the Association are also available on its website at *www.lonestaragcredit.com.* Copies of the Association's quarterly stockholder reports can also be requested by e-mailing *Tonya.Arvin@lonestaragcredit.com.*

LONE STAR, ACA

CONSOLIDATED BALANCE SHEET

	September 30, 2018 (unaudited)	December 31, 2017	September 30, 2017 (unaudited)
ASSETS			
Cash	**$ 415,829**	$ 90,437	$ 347,424
Loans	**1,603,354,136**	1,681,072,602	1,701,198,640
Less: allowance for loan losses	**(9,076,136)**	(9,181,997)	(12,713,033)
Net loans	**1,594,278,000**	1,671,890,605	1,688,485,607
Accrued interest receivable	**10,769,092**	9,321,322	11,112,647
Investment in and receivable from the Farm Credit Bank of Texas:			
Capital stock	**27,562,030**	27,562,030	26,002,180
Other	**4,725,727**	1,334,685	5,027,022
Premises and equipment, net	**2,942,514**	2,835,580	2,926,120
Other assets	**1,380,795**	961,471	1,244,595
Total assets	**$ 1,642,073,987**	$ 1,713,996,130	$ 1,735,145,595
LIABILITIES			
Note payable to the Farm Credit Bank of Texas	**$ 1,271,643,908**	$ 1,358,683,640	$ 1,389,365,902
Accrued interest payable	**2,891,107**	2,807,131	2,647,574
Drafts outstanding	**24,189**	137,903	82,576
Other liabilities	**11,064,666**	11,723,904	9,221,913
Total liabilities	**1,285,623,870**	1,373,352,578	1,401,317,965
MEMBERS' EQUITY			
Capital stock and participation certificates	**6,026,820**	6,386,865	6,426,465
Additional paid-in capital	**91,343,553**	91,343,553	91,343,553
Unallocated retained earnings	**260,393,080**	244,270,903	236,884,455
Accumulated other comprehensive loss	**(1,313,336)**	(1,357,769)	(826,843)
Total members' equity	**356,450,117**	340,643,552	333,827,630
Total liabilities and members' equity	**$ 1,642,073,987**	$ 1,713,996,130	$ 1,735,145,595

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

LONE STAR, ACA

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(unaudited)

	Quarter Ended September 30,		Nine months ended September 30,	
	2018	2017	**2018**	2017
INTEREST INCOME				
Loans	**$ 20,117,461**	$ 19,781,320	**$ 63,616,695**	$ 58,184,030
Total interest income	**20,117,461**	19,781,320	**63,616,695**	58,184,030
INTEREST EXPENSE				
Note payable to the Farm Credit Bank of Texas	**9,055,874**	8,166,519	**26,498,312**	23,001,929
Advance conditional payments	**334**	11	**368**	30
Total interest expense	**9,056,208**	8,166,530	**26,498,680**	23,001,959
Net interest income	**11,061,253**	11,614,790	**37,118,015**	35,182,071
PROVISION FOR LOAN LOSSES	**1,053,563**	2,075,056	**(101,027)**	2,746,464
Net interest income after provision for loan losses	**10,007,690**	9,539,734	**37,219,042**	32,435,607
NONINTEREST INCOME				
Income from the Farm Credit Bank of Texas:				
Patronage income	**1,662,908**	1,602,030	**4,825,119**	4,748,814
Loan fees	**80,772**	47,813	**226,922**	244,274
Financial-related services income	**1,113**	1,776	**5,496**	6,374
Gain (loss) on other property owned, net	**-**	14,004	**26,318**	39,134
Gain (loss) on sale of premises and equipment, net	**182,577**	121	**263,045**	(550)
Other noninterest income	**41,475**	61,725	**1,228,455**	288,496
Total noninterest income	**1,968,845**	1,727,469	**6,575,355**	5,326,542
NONINTEREST EXPENSES				
Salaries and employee benefits	**3,400,923**	2,168,858	**10,420,942**	8,931,590
Directors' expense	**118,727**	113,931	**355,306**	377,326
Purchased services	**2,234,830**	7,362,234	**4,735,355**	8,330,655
Travel	**285,858**	235,311	**682,292**	634,669
Occupancy and equipment	**325,796**	326,877	**1,086,412**	960,577
Communications	**91,869**	87,226	**278,212**	234,811
Advertising	**159,221**	191,987	**387,310**	533,040
Public and member relations	**231,275**	223,201	**654,065**	768,693
Supervisory and exam expense	**135,356**	164,319	**463,996**	408,114
Insurance Fund premiums	**271,035**	481,641	**834,901**	1,421,341
Other noninterest expense	**278,819**	1,705,999	**705,457**	10,919,882
Total noninterest expenses	**7,533,709**	13,061,584	**20,604,248**	33,520,698
Income before income taxes	**4,442,826**	(1,794,381)	**23,190,149**	4,241,451
Provision for income taxes	**6,189**	13,292	**18,018**	39,956
NET INCOME (LOSS)	**4,436,637**	(1,807,673)	**23,172,131**	4,201,495
Other comprehensive income:				
Change in postretirement benefit plans	**14,811**	2,055	**44,433**	6,165
Other comprehensive income, net of tax	**14,811**	2,055	**44,433**	6,165
COMPREHENSIVE INCOME (LOSS)	**$ 4,451,448**	$ (1,805,618)	**$ 23,216,564**	$ 4,207,660

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

LONE STAR, ACA

CONSOLIDATED STATEMENT OF CHANGES IN MEMBERS' EQUITY

(unaudited)

	Capital Stock/ Participation Certificates	Additional Paid-in-Capital	Unallocated Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
Balance at December 31, 2016	$ 6,431,805	$ 91,343,553	$ 232,668,103	$ (833,008)	$ 329,610,453
Comprehensive income			4,201,495	6,165	4,207,660
Capital stock/participation certificates and allocated retained earnings issued	607,970				607,970
Capital stock/participation certificates and allocated retained earnings retired	(613,310)				(613,310)
Dividend adjustments			14,857		14,857
Balance at September 30, 2017	$ 6,426,465	$ 91,343,553	$ 236,884,455	$ (826,843)	$ 333,827,630
Balance at December 31, 2017	$ 6,386,865	$ 91,343,553	$ 244,270,903	$ (1,357,769)	$ 340,643,552
Comprehensive income			23,172,131	44,433	23,216,564
Capital stock/participation certificates and allocated retained earnings issued	308,510				308,510
Capital stock/participation certificates and allocated retained earnings retired	(668,555)				(668,555)
Patronage refunds:					
Cash			(7,049,954)		(7,049,954)
Balance at September 30, 2018	**$ 6,026,820**	**$ 91,343,553**	**$ 260,393,080**	**$ (1,313,336)**	**$ 356,450,117**

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

NOTE 1 — ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES:

Lone Star, ACA, including its wholly-owned subsidiaries, Lone Star, PCA and Lone Star, FLCA (collectively referred to as "the Association"), is a member-owned cooperative which provides credit and credit-related services to, or for the benefit of, eligible borrowers/stockholders for qualified agricultural purposes in the counties of Bell, Borden, Bosque, Bowie, Burnet, Camp, Cass, Cooke, Coryell, Dallas, Delta, Denton, Eastland, Ellis, Erath, Falls, Fannin, Fisher, Freestone, Grayson, Hamilton, Hill, Hood, Johnson, Kent, Lamar, Lampasas, Limestone, McLennan, Milam, Mitchell, Morris, Navarro, Nolan, Palo Pinto, Parker, Red River, Scurry, Shackelford, Somervell, Stephens, Tarrant, Taylor, Throckmorton, Titus, Williamson, Wise and Young in the state of Texas. The Association is a lending institution of the Farm Credit System ("the System"), which was established by Acts of Congress to meet the needs of American agriculture.

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the U.S. (GAAP) for interim financial information. Accordingly, they do not include all of the disclosures required by GAAP for annual financial statements and should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2017, as contained in the 2017 Annual Report to Stockholders.

In the opinion of management, the accompanying consolidated financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with generally accepted accounting principles (GAAP), except for the inclusion of a statement of cash flows. GAAP require a business enterprise that provides a set of financial statements reporting both financial position and results of operations to also provide a statement of cash flows for each period for which results of operations are provided. In regulations issued by FCA, associations have the option to exclude statements of cash flows in interim financial statements. Therefore, the Association has elected not to include a statement of cash flows in these consolidated financial statements.

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year ending December 31, 2018. In the opinion of management, these policies and the presentation of the interim financial condition and results of operations conform with GAAP and prevailing practices within the banking industry.

In February 2018, the Financial Accounting Standards Board (FASB) issued guidance entitled "Income Statement — Reporting Comprehensive Income — Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income." This guidance allows for the reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the recently issued tax legislation, Tax Cuts and Jobs Act (TCJA) that lowered the federal corporate tax rate from 35% to 21%. The amount of the reclassification shall include the effect of the change in the tax rate on gross deferred tax amounts and related valuation allowances at the date of enactment of the TCJA related to items remaining in accumulated other comprehensive income. The guidance becomes effective for financial statements issued for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted. The Association is evaluating the impact of adoption on the Association's financial condition and its results of operations.

In August 2017, the Financial Accounting Standards Board (FASB) issued guidance entitled "Targeted Improvements to Accounting for Hedging Activities." The guidance better aligns an entity's risk management activities and financial reporting for hedging relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. The amendments in this guidance require an entity to present the earnings effect of the hedging instrument in the same income statement line item in which the earnings effect of the hedged item is reported. This guidance also addresses the timing of effectiveness testing, qualitative and quantitative effectiveness testing and components that can be excluded from effectiveness testing. This guidance becomes effective for interim and annual periods beginning after December 15, 2018. The Association is evaluating the impact of adoption on the Association's financial condition and its results of operations.

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

In August 2016, the FASB issued guidance entitled "Classification of Certain Cash Receipts and Cash Payments." The guidance addresses specific cash flow issues with the objective of reducing the diversity in the classification of these cash flows. Included in

the cash flow issues are debt prepayment or debt extinguishment costs and settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing. This guidance becomes effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance did not impact the Association's financial condition or its results of operations but did change the classification of certain items in the statement of cash flows.

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

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

In January 2016, the FASB issued guidance entitled "Recognition and Measurement of Financial Assets and Liabilities." This guidance affects, among other things, the presentation and disclosure requirements for financial instruments. For public entities, the guidance eliminates the requirement to disclose the methods and significant assumptions used to estimate the fair value of financial instruments carried at amortized cost. This guidance becomes effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance did not impact the Association's financial condition or its results of operations but did impact the Association's fair value disclosures.

In May 2014, the FASB issued guidance entitled, "Revenue from Contracts with Customers." The guidance governs revenue recognition from contracts with customers and requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Financial instruments and other contractual rights within the scope of other guidance issued by the FASB are excluded from the scope of this new revenue recognition guidance. The guidance sets forth the requirement for new and enhanced disclosures. The Association has determined that the effect of the adoption is not material to its financial condition or results of operations and will not change its current recognition practices.

NOTE 2 – RESTATEMENT:

As discussed in the 2017 Annual Report, a breach of the Association's policies and procedures by a former loan officer resulted in certain misstatements in previously issued financial statements for the year ended December 31, 2016 and quarter-ending March 31, 2017. Accordingly, in May of 2018, Lone Star published restated 2016 year-end data within its 2017 Annual Report and published restated March 31, 2017 quarter-ending financials within the Association's March 31, 2018 quarter-end financials issued on May 31, 2018.

NOTE 3 — LOANS AND ALLOWANCE FOR LOAN LOSSES:

A summary of loans follows:

Loan Type	**September 30, 2018 Amount**	December 31, 2017 Amount	September 30, 2017 Amount
Production agriculture:			
Real estate mortgage	**$ 1,272,971,241**	$ 1,349,434,350	$ 1,358,248,199
Production and intermediate term	**98,407,085**	106,690,588	109,087,705
Agribusiness:			
Loans to cooperatives	**18,626,052**	14,281,948	17,734,893
Processing and marketing	**137,413,150**	127,788,252	128,352,365
Farm-related business	**12,856,657**	15,113,769	14,651,728
Communication	**8,610,754**	8,729,168	8,847,302
Energy	**38,628,227**	41,992,131	42,774,525
Water and waste water	**4,747,133**	3,357,911	6,776,049
Rural residential real estate	**11,093,837**	13,684,485	14,725,874
Total	**$ 1,603,354,136**	$ 1,681,072,602	$ 1,701,198,640

The Association purchases or sells 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 the balances of participations purchased and sold at September 30, 2018:

	Other Farm Credit Institutions		Non-Farm Credit Institutions		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 16,088,496	$ 6,491,535	$ -	$ -	$ 16,088,496	$ 6,491,535
Production and intermediate term	42,432,930	-	-	-	42,432,930	-
Agribusiness	155,240,322	-	-	-	155,240,322	-
Communication	8,610,755	-	-	-	8,610,755	-
Energy	38,628,227	-	-	-	38,628,227	-
Water and waste water	3,000,381	-	1,746,752	-	4,747,133	-
Total	$264,001,111	$ 6,491,535	$ 1,746,752	$ -	$265,747,863	$ 6,491,535

The Association is authorized under the Farm Credit Act to accept "advance conditional payments" ("ACPs") from borrowers. To the extent the borrower's access to such ACPs is restricted and the legal right of setoff exists, the ACPs are netted against the borrower's related loan balance. Unrestricted ACPs are included in other liabilities. ACPs are not insured, and interest is generally paid by the Association on such balances. Balances of ACPs were $9,375,560 , $13,111,538 and $17,257,894 at September 30, 2018, December 31, 2017 and September 30, 2017, respectively.

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

	September 30, 2018	December 31, 2017	September 30, 2017
Nonaccrual loans:			
Real estate mortgage	**$ 4,307,840**	$ 3,893,283	$ 4,008,111
Production and intermediate term	**201,581**	1,511,641	1,300,296
Rural residential real estate	**158,387**	228,181	825,647
Total nonaccrual loans	**4,667,808**	5,633,105	6,134,054
Accruing restructured loans:			
Real estate mortgage	**111,414**	3,078,911	3,103,044
Production and intermediate term	**1,459,179**	1,458,427	-
Total accruing restructured loans	**1,570,593**	4,537,338	3,103,044
Accruing loans 90 days or more past due:			
Real estate mortgage	**-**	-	1,327,233
Production and intermediate term	**-**	-	39,423
Total accruing loans 90 days or more past due	**-**	-	1,366,656
Total nonperforming loans	**6,238,401**	10,170,443	10,603,754
Other property owned	**-**	-	-
Total nonperforming assets	**$ 6,238,401**	$ 10,170,443	$ 10,603,754

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

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

The following table shows loans and related accrued interest as a percentage of total loans and related accrued interest receivable by loan type as of:

	September 30, 2018	December 31, 2017	Setember 30, 2017
Real estate mortgage			
Acceptable	**95%**	95%	95%
OAEM	**4%**	4%	4%
Substandard/doubtful	**1%**	1%	1%
	100%	100%	100%
Production and intermediate term			
Acceptable	**92%**	86%	89%
OAEM	**6%**	11%	8%
Substandard/doubtful	**2%**	3%	3%
	100%	100%	100%
Agribusiness			
Acceptable	**100%**	99%	96%
OAEM	**0%**	0%	3%
Substandard/doubtful	**0%**	1%	1%
	100%	100%	100%
Energy and water/waste water			
Acceptable	**98%**	98%	98%
OAEM	**2%**	2%	2%
Substandard/doubtful	**0%**	0%	0%
	100%	100%	100%
Communication			
Acceptable	**100%**	100%	100%
OAEM	**0%**	0%	0%
Substandard/doubtful	**0%**	0%	0%
	100%	100%	100%
Rural residential real estate			
Acceptable	**96%**	95%	92%
OAEM	**1%**	1%	1%
Substandard/doubtful	**3%**	4%	7%
	100%	100%	100%
Total loans			
Acceptable	**95%**	95%	95%
OAEM	**4%**	4%	4%
Substandard/doubtful	**1%**	1%	1%
	100%	100%	100%

The following tables provide an age analysis of past due loans (including accrued interest) as of:

September 30, 2018	**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**
Real estate mortgage	**$ 2,456,310**	**$ 658,625**	**$ 3,114,935**	**$ 1,279,267,540**	**$ 1,282,382,475**
Production and intermediate term	**305,399**	**134,979**	**440,378**	**98,820,402**	**99,260,780**
Loans to cooperatives	**-**	**-**	**-**	**18,654,664**	**18,654,664**
Processing and marketing	**-**	**-**	**-**	**137,649,654**	**137,649,654**
Farm-related business	**-**	**-**	**-**	**12,912,896**	**12,912,896**
Communication	**-**	**-**	**-**	**8,613,703**	**8,613,703**
Energy	**-**	**-**	**-**	**38,769,770**	**38,769,770**
Water and waste water	**-**	**-**	**-**	**4,752,759**	**4,752,759**
Rural residential real estate	**-**	**121,085**	**121,085**	**11,005,442**	**11,126,527**
Total	**$ 2,761,709**	**$ 914,689**	**$ 3,676,398**	**$ 1,610,446,830**	**$ 1,614,123,228**

December 31, 2017	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans
Real estate mortgage	$ 2,631,648	$ 846,122	$ 3,477,770	$ 1,354,146,638	$ 1,357,624,408
Production and intermediate term	131,182	1,302,507	1,433,689	105,968,882	107,402,571
Loans to cooperatives	-	-	-	14,295,656	14,295,656
Processing and marketing	-	-	-	127,947,843	127,947,843
Farm-related business	-	-	-	15,154,992	15,154,992
Communication	-	-	-	8,731,512	8,731,512
Energy	-	-	-	42,156,596	42,156,596
Water and waste water	-	-	-	3,362,464	3,362,464
Rural residential real estate	209,009	92,443	301,452	13,416,430	13,717,882
Total	$ 2,971,839	$ 2,241,072	$ 5,212,911	$ 1,685,181,013	$ 1,690,393,924

September 30, 2017	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans
Real estate mortgage	$ 2,505,447	$ 2,158,212	$ 4,663,659	$ 1,363,057,104	$ 1,367,720,763
Production and intermediate term	5,854,293	906,778	6,761,071	103,417,841	110,178,912
Loans to cooperatives	-	-	-	17,761,816	17,761,816
Processing and marketing	-	-	-	128,568,691	128,568,691
Farm-related business	-	-	-	14,722,166	14,722,166
Communication	-	-	-	8,864,264	8,864,264
Energy	-	-	-	42,944,139	42,944,139
Water and waste water	-	-	-	6,787,232	6,787,232
Rural residential real estate	92,765	676,283	769,048	13,994,256	14,763,304
Total	$ 8,452,505	$ 3,741,273	$ 12,193,778	$ 1,700,117,509	$ 1,712,311,287

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 September 30, 2018, the total recorded investment of troubled debt restructured loans was $2,373,085, including $802,492 classified as nonaccrual and $1,570,593 classified as accrual, with specific allowance for loan losses of $162,057. As of September

30, 2018, commitments to lend funds to borrowers whose loan terms have been modified in a troubled debt restructuring were $0 at period end and $0 at December 31, 2017 and September 30, 2017.

The following tables present additional information regarding troubled debt restructurings, which includes both accrual and nonaccrual loans with troubled debt restructuring designation, that occurred during the nine months ended September 30, 2018. 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. Loans formally restructured prior to January 1, 2018, were $1,875,753.

For the Three Months Ended September 30, 2018	Premodification Outstanding Recorded Investment	Postmodification Outstanding Recorded Investment
Troubled debt restructurings:		
Real estate mortgage	$ 201,506	$ 201,506
Rural residential real estate	120,213	121,085
Total	$ 321,719	$ 322,591

There were no loans with troubled debt restructuring designation that occurred during the three months ended September 30, 2017.

For the Nine Months Ended September 30, 2018	Premodification Outstanding Recorded Investment	Postmodification Outstanding Recorded Investment
Troubled debt restructurings:		
Real estate mortgage	$ 381,922	$ 376,428
Rural residential real estate	120,213	121,085
Total	$ 502,135	$ 497,513

There were no loans with troubled debt restructuring designation that occurred during the nine months ended September 30, 2017.

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 restructurings where principal was forgiven that required a charge off, at the modification date, for the three months and nine months ending September 30, 2018 and 2017, respectively.

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

At September 30, 2018, December 31, 2017 and September 30, 2017, the Association had no 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.

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

	Loans Modified as TDRs			TDRs in Nonaccrual Status*		
	September 30, 2018	December 31, 2017	September 30, 2017	September 30, 2018	December 31, 2017	September 30, 2017
Real estate mortgage	$ 679,315	$ 3,297,717	$ 3,329,236	$ 567,900	$ 218,806	$ 226,192
Production and intermediate term	1,572,685	1,708,217	-	113,507	249,790	-
Rural residential real estate	121,085	-	-	121,085	-	-
Total	$ 2,373,085	$ 5,005,934	$ 3,329,236	$ 802,492	$ 468,596	$ 226,192

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

Additional impaired loan information is as follows:

	September 30, 2018			December 31, 2017			September 30, 2017		
	Recorded Investment	**Unpaid Principal Balance[a]**	**Related Allowance**	Recorded Investment	Unpaid Principal Balance[a]	Related Allowance	Recorded Investment	Unpaid Principal Balance[a]	Related Allowance
Impaired loans with a related allowance for credit losses:									
Real estate mortgage	**$ 863,112**	**$ 974,275**	**$ 219,141**	$ 160,483	$ 214,343	$ 46,363	$ 998,675	$ 1,001,725	$ 115,598
Production and intermediate term	**193,222**	**435,248**	**52,852**	797,585	1,465,175	302,611	1,257,593	1,513,869	591,730
Rural residential real estate	**121,084**	**168,942**	**49,012**	-	-	-	676,283	675,983	65,568
Total	**$1,177,418**	**$ 1,578,465**	**$ 321,005**	$ 958,068	$ 1,679,518	$ 348,974	$ 2,932,551	$ 3,191,577	$ 772,896
Impaired loans with no related allowance for credit losses:									
Real estate mortgage	**$3,556,143**	**$ 3,611,217**	**$ -**	$ 6,811,711	$ 6,810,197	$ -	$ 7,439,714	$ 7,405,072	$ -
Production and intermediate term	**1,467,538**	**2,540,055**	**-**	2,172,484	2,797,932	-	82,125	947,358	-
Rural residential real estate	**37,302**	**37,498**	**-**	228,181	228,377	-	149,364	149,860	-
Total	**$5,060,983**	**$ 6,188,770**	**$ -**	$ 9,212,376	$ 9,836,506	$ -	$ 7,671,203	$ 8,502,290	$ -
Total impaired loans:									
Real estate mortgage	**$4,419,255**	**$ 4,585,492**	**$ 219,141**	$ 6,972,194	$ 7,024,540	$ 46,363	$ 8,438,389	$ 8,406,797	$ 115,598
Production and intermediate term	**1,660,760**	**2,975,303**	**52,852**	2,970,069	4,263,107	302,611	1,339,718	2,461,227	591,730
Rural residential real estate	**158,386**	**206,440**	**49,012**	228,181	228,377	-	825,647	825,843	65,568
Total	**$6,238,401**	**$ 7,767,235**	**$ 321,005**	$ 10,170,444	$ 11,516,024	$ 348,974	$ 10,603,754	$ 11,693,867	$ 772,896

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

	For the Three Months Ended				For the Nine Months Ended			
	September 30, 2018		September 30, 2017		**September 30, 2018**		September 30, 2017	
	Average Impaired Loans	**Interest Income Recognized**	Average Impaired Loans	Interest Income Recognized	**Average Impaired Loans**	**Interest Income Recognized**	Average Impaired Loans	Interest Income Recognized
Impaired loans with a related allowance for credit losses:								
Real estate mortgage	**$ 862,284**	**$ -**	$ 1,006,238	$ -	**$ 530,847**	**$ 11,207**	$ 566,471	$ 10,833
Production and intermediate term	**195,603**	**-**	1,327,899	-	**395,663**	**2,325**	1,086,263	9,043
Farm-related business	**-**	**-**	-	-	**-**	**-**	-	-
Rural residential real estate	**120,624**	**-**	675,356	-	**59,982**	**2,243**	245,828	-
Total	**$1,178,511**	**$ -**	$ 3,009,493	$ -	**$ 986,492**	**$ 15,775**	$ 1,898,562	$ 19,876
Impaired loans with no related allowance for credit losses:								
Real estate mortgage	**$3,597,585**	**$ 4,433**	$ 7,393,262	$ 276,070	**$ 4,592,254**	**$ 23,085**	$ 7,476,949	$ 835,925
Production and intermediate term	**1,489,201**	**27,076**	607,382	553	**1,643,249**	**86,170**	978,263	2,304
Farm-related business	**-**	**1,844**	-	12,896	**-**	**10,647**	-	16,951
Rural residential real estate	**39,271**	**-**	154,477	-	**45,201**	**-**	624,196	-
Total	**$5,126,057**	**$ 33,353**	$ 8,155,121	$ 289,519	**$ 6,280,704**	**$ 119,902**	$ 9,079,408	$ 855,180
Total impaired loans:								
Real estate mortgage	**$4,459,869**	**$ 4,433**	$ 8,399,500	$ 276,070	**$ 5,123,101**	**$ 34,292**	$ 8,043,420	$ 846,758
Production and intermediate term	**1,684,804**	**27,076**	1,935,281	553	**2,038,912**	**88,495**	2,064,526	11,347
Farm-related business	**-**	**1,844**	-	12,896	**-**	**10,647**	-	16,951
Rural residential real estate	**159,895**	**-**	829,833	-	**105,183**	**2,243**	870,024	-
Total	**$6,304,568**	**$ 33,353**	$11,164,614	$ 289,519	**$ 7,267,196**	**$ 135,677**	$ 10,977,970	$ 875,056

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

	Real Estate Mortgage	Production and Intermediate Term	Agribusiness	Communications	Energy and Water/Waste Water	Rural Residential Real Estate	Total
Allowance for Credit Losses:							
Balance at June 30, 2018	$ 5,842,098	$ 1,218,325	$ 500,664	$ 11,909	$ 186,075	$ 107,302	$ 7,866,373
Charge-offs	-	(124,270)	-	-	-	-	(124,270)
Recoveries	-	200,722	76,826	-	-	-	277,548
Provision for loan losses	886,218	329,372	(179,754)	55	22,652	(4,980)	1,053,563
Other	(857)	6,692	(7,442)	54	4,475	-	2,922
Balance at September 30, 2018	$ 6,727,459	$ 1,630,841	$ 390,294	$ 12,018	$ 213,202	$ 102,322	$ 9,076,136
Balance at December 31, 2017	$ 6,775,679	$ 1,510,355	$ 530,851	$ 15,578	$ 188,448	$ 161,086	$ 9,181,997
Charge-offs	(108,113)	(484,991)	-	-	-	(47,857)	(640,961)
Recoveries	-	253,317	220,078	-	-	-	473,395
Provision for loan losses	56,303	218,950	(378,812)	(3,546)	16,985	(10,907)	(101,027)
Other	3,590	133,210	18,177	(14)	7,769	-	162,732
Balance at September 30, 2018	$ 6,727,459	$ 1,630,841	$ 390,294	$ 12,018	$ 213,202	$ 102,322	$ 9,076,136
Ending Balance:							
Individually evaluated for impairment	$ 52,852	$ 219,141	$ -	$ -	$ -	$ 49,012	$ 321,005
Collectively evaluated for impairment	6,674,607	1,411,700	390,294	12,018	213,202	53,310	8,755,131
Loans acquired with deteriorated credit quality	-	-	-	-	-	-	-
Balance at September 30, 2018	$ 6,727,459	$ 1,630,841	$ 390,294	$ 12,018	$ 213,202	$ 102,322	$ 9,076,136
Balance at June 30, 2017	$ 7,242,820	$ 2,801,120	$ 609,588	$ 14,644	$ 146,353	$ 67,876	$ 10,882,401
Charge-offs	-	(332,791)	-	-	-	-	(332,791)
Recoveries	-	58,665	152,926	-	-	-	211,591
Provision for loan losses	2,255,695	(98,840)	(171,792)	569	16,712	72,712	2,075,056
Other	(135,076)	2,016	5,510	568	3,758	-	(123,224)
Balance at September 30, 2017	$ 9,363,439	$ 2,430,170	$ 596,232	$ 15,781	$ 166,823	$ 140,588	$ 12,713,033
Balance at December 31, 2016	$ 7,306,321	$ 1,966,085	$ 584,077	$ 14,320	$ 138,081	$ 62,863	$ 10,071,747
Charge-offs	(61,673)	(423,797)	-	-	-	-	(485,470)
Recoveries	19,232	95,344	386,650	-	-	-	501,226
Provision for loan losses	2,234,307	790,823	(381,242)	732	24,119	77,725	2,746,464
Other	(134,748)	1,715	6,747	729	4,623	-	(120,934)
Balance at September 30, 2017	$ 9,363,439	$ 2,430,170	$ 596,232	$ 15,781	$ 166,823	$ 140,588	$ 12,713,033
Ending Balance:							
Individually evaluated for impairment	$ 115,598	$ 591,730	$ -	$ -	$ -	$ 65,568	$ 772,896
Collectively evaluated for impairment	9,247,841	1,838,440	596,232	15,781	166,823	75,020	11,940,137
Loans acquired with deteriorated credit quality	-	-	-	-	-	-	-
Balance at September 30, 2017	$ 9,363,439	$ 2,430,170	$ 596,232	$ 15,781	$ 166,823	$ 140,588	$ 12,713,033

	Real Estate Mortgage	Production and Intermediate Term	Agribusiness	Communications	Energy and Water/Waste Water	Rural Residential Real Estate	Total
Recorded Investments in Loans Outstanding:							
Ending Balance at September 30, 2018	$1,282,382,474	$ 99,260,781	$169,217,214	$ 8,613,703	$ 43,522,529	$ 11,126,527	$1,614,123,228
Individually evaluated for impairment	$ 4,419,254	$ 1,660,760	$ -	$ -	$ -	$ 158,387	$ 6,238,401
Collectively evaluated for impairment	$1,277,963,220	$ 97,600,021	$169,217,214	$ 8,613,703	$ 43,522,529	$ 10,968,140	$1,607,884,827
Loans acquired with deteriorated credit quality	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Ending Balance at December 31, 2017	$1,357,624,407	$ 107,402,571	$157,398,491	$ 8,713,512	$ 45,519,060	$ 13,717,883	$1,690,375,924
Individually evaluated for impairment	$ 6,950,507	$ 2,970,069	$ -	$ -	$ -	$ 228,182	$ 10,148,758
Collectively evaluated for impairment	$1,350,652,214	$ 104,432,502	$157,398,491	$ 8,713,512	$ 45,519,060	$ 13,489,701	$1,680,205,480
Loans acquired with deteriorated credit quality	$ 21,686	$ -	$ -	$ -	$ -	$ -	$ 21,686
Ending Balance at September 30, 2017	$1,367,720,763	$ 110,178,912	$161,052,673	$ 8,864,264	$ 49,731,371	$ 14,763,304	$1,712,311,287
Individually evaluated for impairment	$ 7,111,155	$ 1,300,296	$ -	$ -	$ -	$ 825,647	$ 9,237,098
Collectively evaluated for impairment (restated)	$1,360,609,608	$ 108,878,616	$161,052,673	$ 8,864,264	$ 49,731,371	$ 13,937,657	$1,703,074,189
Loans acquired with deteriorated credit quality	$ -	$ -	$ -	$ -	$ -	$ -	$ -

NOTE 4 — CAPITAL:

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

Regulatory Capitalization Requirements

Risk-adjusted:	Regulatory Minimums	Conservation Buffer	Total	As of September 30, 2018
Common equity tier 1 ratio	4.50%	2.50%	7.00%	19.29%
Tier 1 capital ratio	6.00%	2.50%	8.50%	19.29%
Total capital ratio	8.00%	2.50%	10.50%	19.77%
Permanent capital ratio	7.00%	0.00%	7.00%	19.38%
Non-risk-adjusted:				
Tier 1 leverage ratio	4.00%	1.00%	5.00%	20.03%
UREE leverage ratio	1.50%	0.00%	1.50%	21.34%

Risk-adjusted:	Regulatory Minimums	Conservation Buffer	Total	As of September 30, 2017
Common equity tier 1 ratio	4.50%	2.50%	7.00%	18.16%
Tier 1 capital ratio	6.00%	2.50%	8.50%	18.16%
Total capital ratio	8.00%	2.50%	10.50%	18.65%
Permanent capital ratio	7.00%	0.00%	7.00%	18.25%
Non-risk-adjusted:				
Tier 1 leverage ratio	4.00%	1.00%	5.00%	18.98%
UREE leverage ratio	1.50%	0.00%	1.50%	20.12%

Risk-adjusted assets have been defined by FCA Regulations 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 which 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 (referred herein as PCR risk-adjusted assets) 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 ratio is statutory minimum purchased borrower stock, other required borrower stock held for a minimum of 7 years, allocated equities held for a minimum of 7 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, and 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 5 years, allocated equities held for a minimum of 5 years, subordinated debt and limited-life preferred stock greater than 5 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 (PCR) is all at-risk borrower stock, any allocated excess stock, unallocated retained earnings, paid-in capital, subordinated debt and preferred subject to certain limitations, less certain allocated and purchased investments in other System institutions, divided by PCR 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 minimum regulatory requirements, including the capital conservation and leverage buffer amounts, capital distributions (equity redemptions, dividends, and patronage) and discretionary bonus payments to senior officers 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 September 30, 2018:

(dollars in thousands)	Common Equity Tier 1 ratio	Tier 1 Capital Ratio	Total Capital Ratio	Permanent Capital Ratio
Numerator:				
Unallocated retained earnings	**190,951,573**	**190,951,573**	**190,951,573**	**190,951,573**
Paid-in capital	**91,343,553**	**91,343,553**	**91,343,553**	**91,343,553**
Common Cooperative Equities:				
Statutory minimum purchased borrower stock	**6,111,661**	**6,111,661**	**6,111,661**	**6,111,661**
Nonqualified allocated equities not subject to retirement	**65,733,966**	**65,733,966**	**65,733,966**	**65,733,966**
Allowance for loan losses and reserve for credit losses subject to certain limitations	**-**	**-**	**8,188,122**	**-**
Regulatory Adjustments and Deductions:				
Amount of allocated investments in other System institutions	**(27,562,030)**	**(27,562,030)**	**(27,562,030)**	**(27,562,030)**
	326,578,723	**326,578,723**	**334,766,845**	**326,578,723**
Denominator:				
Risk-adjusted assets excluding allowance	**1,720,785,423**	**1,720,785,423**	**1,720,785,423**	**1,720,785,423**
Regulatory Adjustments and Deductions:				
Regulatory deductions included in total capital	**(27,562,030)**	**(27,562,030)**	**(27,562,030)**	**(27,562,030)**
Allowance for loan losses	**-**	**-**	**-**	**(8,018,888)**
	1,693,223,393	**1,693,223,393**	**1,693,223,393**	**1,685,204,505**

The components of the Association's risk-adjusted capital, based on 90 day average balances, were as follows at September 30, 2017:

(dollars in thousands)	Common Equity Tier 1 ratio	Tier 1 Capital Ratio	Total Capital Ratio	Permanent Capital Ratio
Numerator:				
Unallocated retained earnings	188,118,607	188,118,607	188,118,607	188,118,607
Paid-in capital	91,343,553	91,343,553	91,343,553	91,343,553
Common Cooperative Equities:				
Statutory minimum purchased borrower stock	6,453,691	6,453,691	6,453,691	6,453,691
Nonqualified allocated equities not subject to retirement	65,733,966	65,733,966	65,733,966	65,733,966
Allowance for loan losses and reserve for credit losses subject to certain limitations	-	-	8,693,930	-
Regulatory Adjustments and Deductions:				
Amount of allocated investments in other System institutions	(26,001,180)	(26,001,180)	(26,001,180)	(26,001,180)
Other regulatory required deductions				
	325,648,637	325,648,637	334,342,567	325,648,637
Denominator:				
Risk-adjusted assets excluding allowance	1,819,155,330	1,819,155,330	1,819,155,330	1,819,155,330
Regulatory Adjustments and Deductions:				
Regulatory deductions included in total capital	(26,001,180)	(26,001,180)	(26,001,180)	(26,001,180)
Allowance for loan losses	-	-	-	(8,476,700)
	1,793,154,150	1,793,154,150	1,793,154,150	1,784,677,450

The components of the Association's nonrisk-adjusted capital, based on 90 day average balances, were as follows at September 30, 2018:

(dollars in thousands)	Tier 1 Leverage Ratio	UREE Leverage Ratio
Numerator:		
Unallocated retained earnings	**190,951,573**	**190,951,573**
Paid-in capital	**91,343,553**	**91,343,553**
Common Cooperative Equities:		
Statutory minimum purchased borrower stock	**6,111,661**	**-**
Nonqualified allocated equities not subject to retirement	**65,733,966**	**65,733,966**
Regulatory Adjustments and Deductions:		
Amount of allocated investments in other System institutions	**(27,562,030)**	**(1,000)**
Other regulatory required deductions		
	326,578,723	**348,028,092**
Denominator:		
Total Assets	**1,661,162,374**	**1,661,162,374**
Regulatory Adjustments and Deductions:		
Regulatory deductions included in tier 1 capital	**(30,393,527)**	**(30,393,527)**
	1,630,768,847	**1,630,768,847**

The components of the Association's nonrisk-adjusted capital, based on 90 day average balances, were as follows at September 30, 2017:

(dollars in thousands)	Tier 1 Leverage Ratio	UREE Leverage Ratio
Numerator:		
Unallocated retained earnings	188,118,607	188,118,608
Paid-in capital	91,343,553	91,343,553
Common Cooperative Equities:		
Statutory minimum purchased borrower stock	6,453,691	-
Nonqualified allocated equities not subject to retirement	65,733,966	65,733,966
Regulatory Adjustments and Deductions:		
Amount of allocated investments in other System institutions	(26,001,180)	-
Other regulatory required deductions		
	325,648,637	345,196,127
Denominator:		
Total Assets	1,741,628,166	1,741,628,166
Regulatory Adjustments and Deductions:		
Regulatory deductions included in tier 1 capital	(26,001,180)	(26,001,180)
	1,715,626,986	1,715,626,986

An additional component of equity is accumulated other comprehensive income, which is reported net of taxes, is as follows:

September 30, 2018	**Before Tax**	**Deferred Tax**	**Net of Tax**
Non-pension postretirement benefits	**$ 44,433**	**$ -**	**$ 44,433**
Total	**$ 44,433**	**$ -**	**$ 44,433**

September 30, 2017	Before Tax	Deferred Tax	Net of Tax
Non-pension postretirement benefits	$ 6,165	$ -	$ 6,165
Total	$ 6,165	$ -	$ 6,165

The Association's accumulated other comprehensive income (loss) relates entirely to its non-pension postretirement benefits. Amortization of prior service credit and actuarial losses are reflected in "Salaries and employee benefits" in the Consolidated Statement of Comprehensive Income. The following table summarizes the changes in accumulated other comprehensive income (loss) for the three months ended September 30:

	2018	**2017**
Accumulated other comprehensive loss at January 1	**$ (1,357,769)**	$ (833,008)
Amortization of prior service credits included in salaries and employee benefits	**(19,551)**	(26,066)
Amortization of actuarial loss included in salaries and employee benefits	**63,984**	32,231
Other comprehensive income, net of tax	**44,433**	6,165
Accumulated other comprehensive income at September 30	**$ (1,313,336)**	$ (826,843)

NOTE 5 — INCOME TAXES:

Lone Star, ACA conducts its business activities through two wholly-owned subsidiaries. Long-term mortgage lending activities are conducted through a wholly-owned FLCA subsidiary which is exempt from federal and state income tax. Short- and intermediate-term lending activities are conducted through a wholly-owned PCA subsidiary. The PCA subsidiary and the ACA holding company are subject to income tax. Lone Star, ACA operates as a cooperative that qualifies for tax treatment under Subchapter T of the Internal Revenue Code. Accordingly, under specified conditions, Lone Star, ACA can exclude from taxable income amounts distributed as qualified patronage dividends in the form of cash, stock or allocated retained earnings. Provisions for income taxes are made only on those taxable earnings that will not be distributed as qualified patronage dividends. Deferred taxes are recorded at the tax effect of all temporary differences based on the assumption that such temporary differences are retained by the institution and will therefore impact future tax payments. A valuation allowance is provided against deferred tax assets to the extent that it is more likely than not (more than 50 percent probability), based on management's estimate, that they will not be realized.

NOTE 6 — FAIR VALUE MEASUREMENTS:

FASB guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability. See Note 15 to the 2017 Annual Report to Stockholders for a more complete description.

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

September 30, 2018	**Fair Value Measurement Using**			**Total Fair**
	Level 1	**Level 2**	**Level 3**	**Value**
Assets:				
Assets held in nonqualified benefit trusts	**$174,214**	**$ -**	**$ -**	**174,214**
Total assets	**174,214**	**-**	**-**	**174,214**

December 31, 2017	Fair Value Measurement Using			Total Fair
	Level 1	Level 2	Level 3	Value
Assets:				
Assets held in nonqualified benefit trusts	$ 164,094	$ -	$ -	164,094
Total assets	164,094	-	-	164,094

September 30, 2017	Fair Value Measurement Using			Total Fair
	Level 1	Level 2	Level 3	Value
Assets:				
Assets held in nonqualified benefit trusts	$ 157,935	$ -	$ -	$ 157,935
Total assets	157,935	-	-	157,935

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

September 30, 2018	**Fair Value Measurement Using**			**Total Fair**	**Total Gains**
	Level 1	**Level 2**	**Level 3**	**Value**	**(Losses)**
Assets:					
Loans*	**$ -**	**$ -**	**$ 856,413**	**$ 856,413**	**$ -**

December 31, 2017	Fair Value Measurement Using			Total Fair	Total Gains
	Level 1	Level 2	Level 3	Value	(Losses)
Assets:					
Loans*	$ -	$ -	$ 609,094	$ 609,094	$ -

September 30, 2017	Fair Value Measurement Using			Total Fair	Total Gains
	Level 1	Level 2	Level 3	Value	(Losses)
Assets:					
Loans*	$ -	$ -	$2,151,307	$ 2,151,307	$ -

*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.

Valuation Techniques

As more fully discussed in Note 2 to the 2017 Annual Report to Stockholders, authoritative guidance establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following represent a brief summary of the valuation techniques used for the Association's assets and liabilities. For a more complete description, see Notes to the 2017 Annual Report to Stockholders.

Investment Securities

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

Assets Held in Nonqualified Benefits Trusts

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

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.

Loans

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

Other Property Owned

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

The fair value of commitments is estimated using the fees currently charged for similar agreements, taking into account the remaining terms of the agreements and the creditworthiness of the counterparties. For fixed-rate loan commitments, estimated fair value also considers the difference between current levels of interest rates and the committed rates.

NOTE 7 — EMPLOYEE BENEFIT PLANS:

The following table summarizes the components of net periodic benefit costs of non-pension other postretirement employee benefits for the three months ended September 30:

	Other Benefits	
	2018	2017
Service cost	**$ 67,244**	$ 58,303
Interest cost	**161,551**	158,612
Amortization of prior service (credits) costs	**(26,068)**	(26,068)
Amortization of net actuarial (gain) loss	**32,228**	36,527
Net periodic benefit cost	**$ 234,955**	$ 227,374

The Association's liability for the unfunded accumulated obligation for these benefits at September 30, 2018 and 2017, was $5,563,718 and $4,878,350 , respectively, and is included in "Other Liabilities" in the balance sheet.

The components of net periodic benefit cost other than the service cost component are included in the line item "other components of net periodic postretirement benefit cost" in the income statement.

The structure of the district's defined benefit pension plan is characterized as multiemployer since the assets, liabilities and cost of the plan are not segregated or separately accounted for by participating employers (Bank and associations). The Association recognizes its amortized annual contributions to the plan as an expense. The Association previously disclosed in its financial statements for the year ended December 31, 2017, that it expected to contribute $160,964 to the district's defined benefit pension plan in 2018. As of September 30, 2018, $558,700 of contributions have been made. The Association presently anticipates contributing an additional $186,233 to fund the defined benefit pension plan in 2018 for a total of $744,933 .

NOTE 8 — COMMITMENTS AND CONTINGENT LIABILITIES:

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

NOTE 9 — SUBSEQUENT EVENTS:

The Association has evaluated subsequent events through November 9, 2018, which is the date the financial statements were issued. On November 7, 2018 the Association's CEO, Troy Bussmeir, stepped down at the request of the Board of Directors. The Board of

Directors appointed Interim CEO, William ‘Bill’ Melton, on November 8, 2018. There are no other significant events requiring disclosure as of November 9, 2018