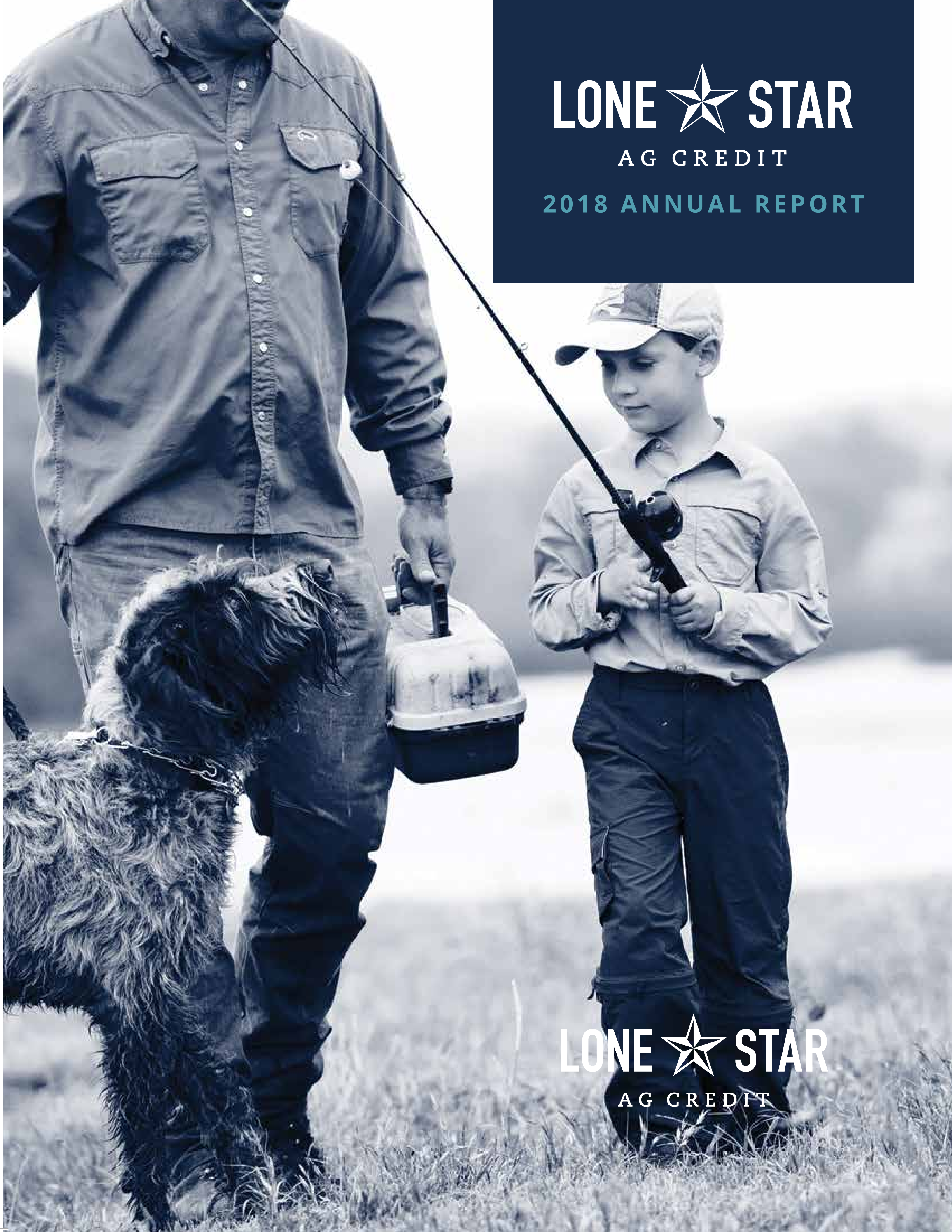
LONE STAR AG CREDIT

2018 ANNUAL REPORT



WE'RE GIVING $20 MILLION BACK TO OUR CUSTOMERS

2018 PATRONAGE FACTS

$20.3 IS LSAC'S LARGEST DISTRIBUTION IN ITS HISTORY.

EQUIVALENT TO 150 BASIS POINTS*

REDUCES EFFECTIVE INTEREST RATE BY 1.5% POINTS*

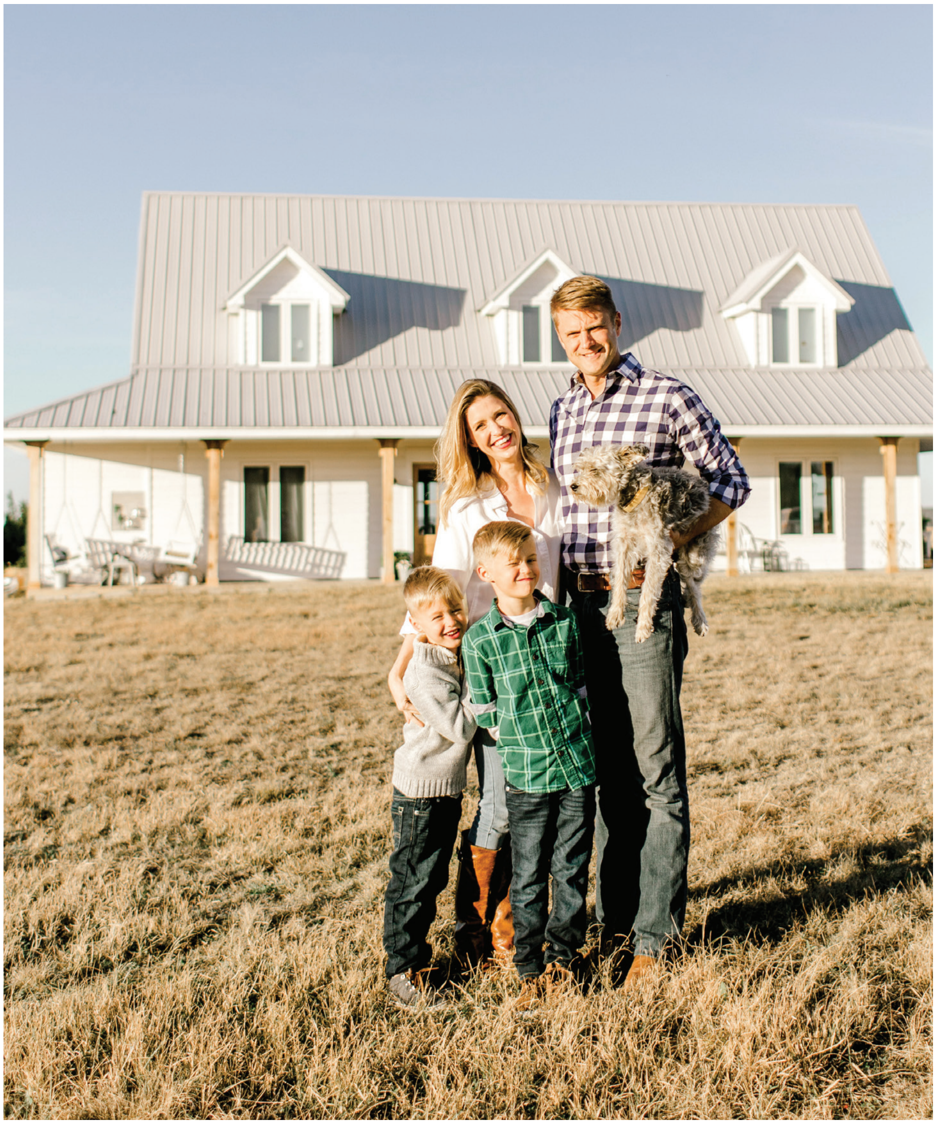
$122 MILLION RETURNED TO OUR INVESTORS SINCE 2000!

*ON AVERAGE

THE AARS FAMILY MOVES TO

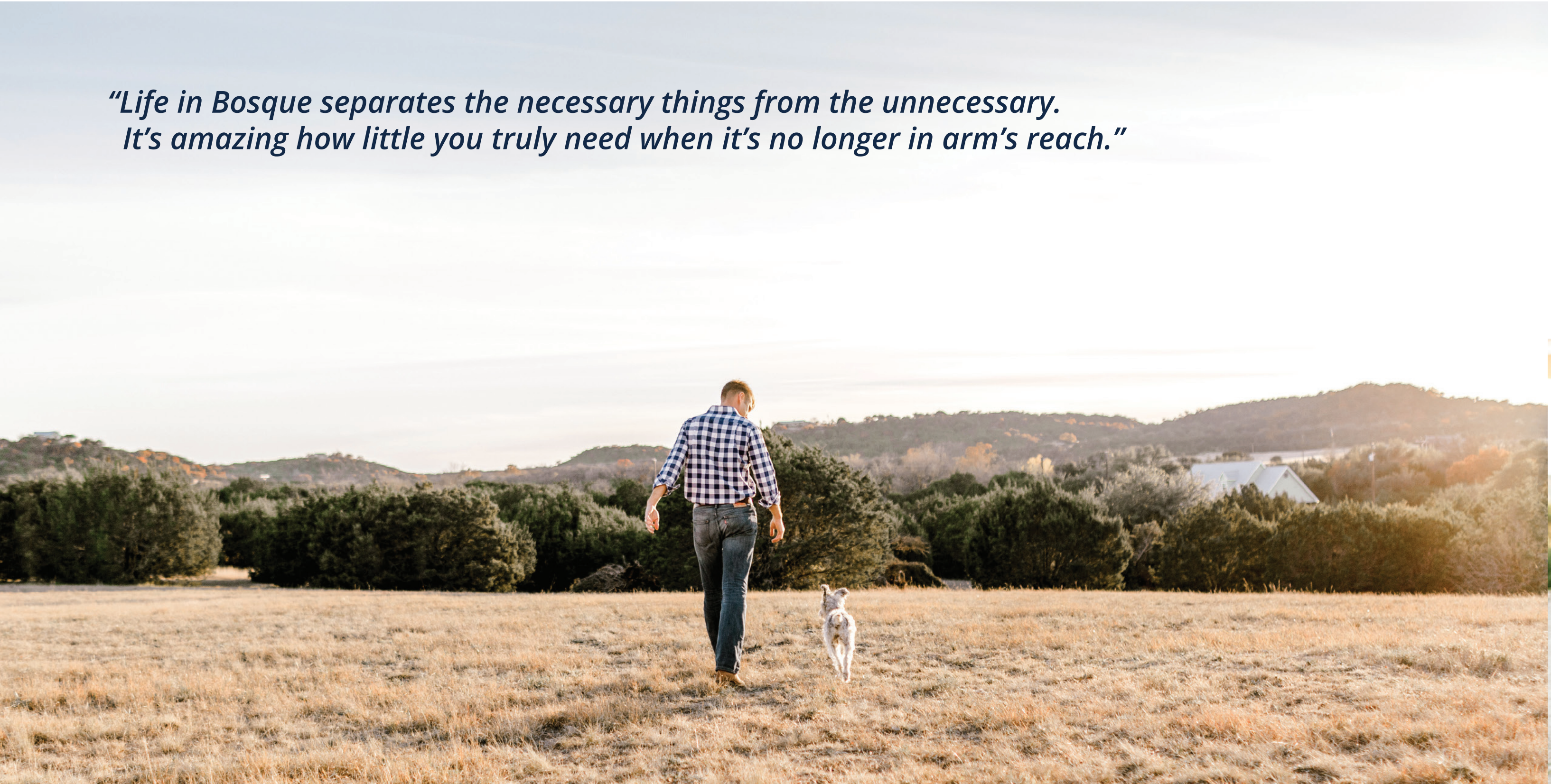
THE FESTIVE FARMHOUSE

Michael and Allison Aars had a busy life in Dallas between work, church, and two active boys. In the back of their minds was the idea of retiring to the Hill Country "one day". Michael's family is from Clifton and Allison's parents have inherited her grandparents' home in Norse, so it was an idea fueled by a desire for their boys to experience the same childhood joys of visiting Norse and exploring the Hill Country. Then, a spontaneous weekend drive along Bosque County backroads set their dream of living in the country in motion.



Michael + Allison Aars Family.
Photo: Kaitlyn Bullard/The Big and Bright

"Life in Bosque separates the necessary things from the unnecessary. It's amazing how little you truly need when it's no longer in arm's reach."

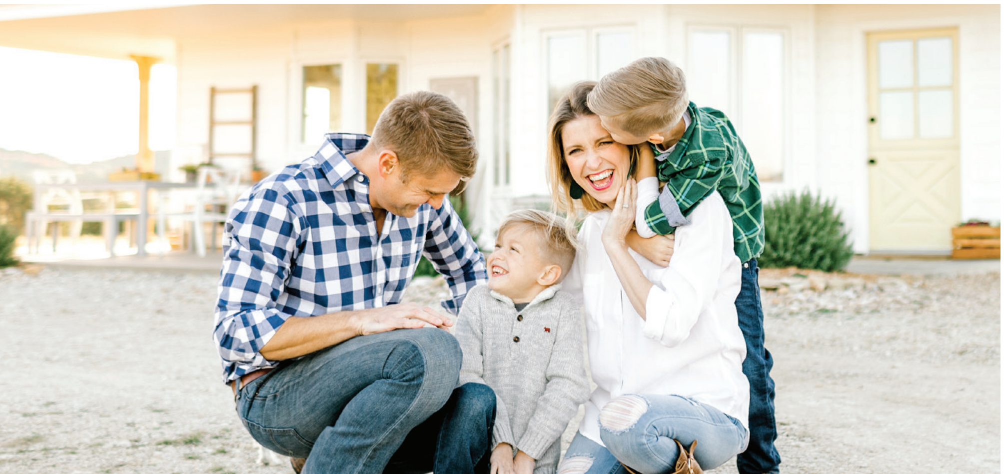


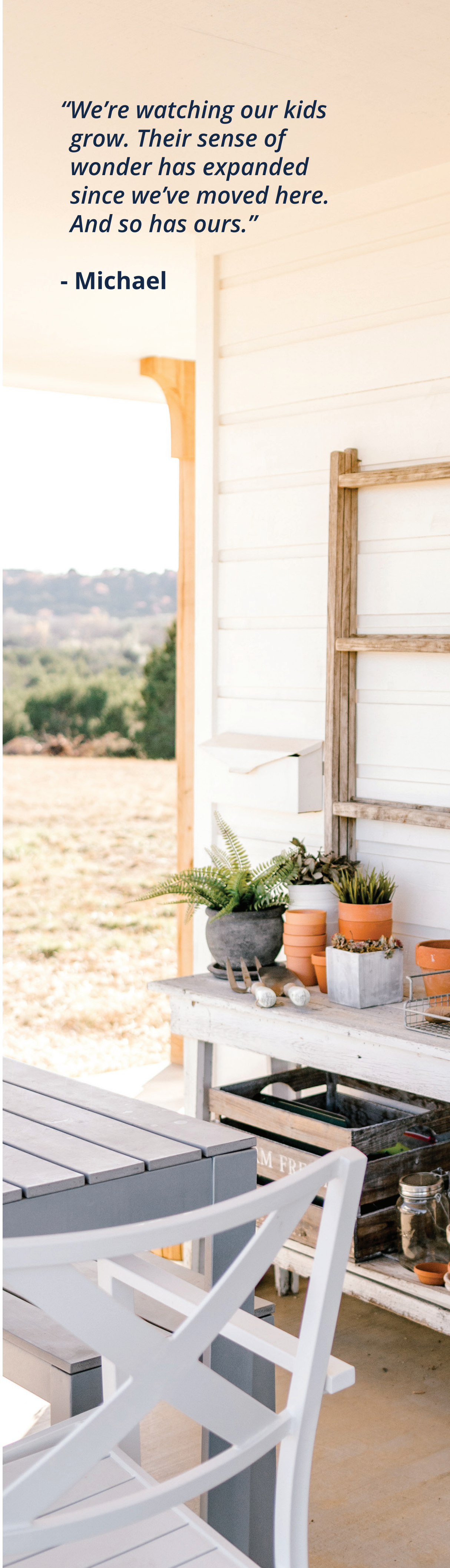
“You know how weather events are classified as Acts of God? That’s pretty much how this move went. We spotted a real estate sign, locked up wheels and 30 days later, we were buying a farm!“ said Allison. “The property felt like it was made for us. The boys were splashing in the creek and when we asked if they wanted to move, their giddy laughter sealed the decision.”

The Aars initially planned to call their lending contacts in Dallas, but found out that buying agricultural land is different. Their realtor suggested Justin Kelly at Lone Star Ag Credit, and he walked the Aars through the differences of small acreage versus large, and became a trusted resource.

“Justin absolutely guided us through the process, and he never ‘let the fish off the line,’ so to speak. It was through his expertise and engaged support that we secured the loan for what we now call home, a festive farmhouse with 32 acres in Bosque County,” said Michael. “Now I get together with Justin for breakfast once in a while and trade success secrets. ‘Do you have a good fencing guy? What animals are you thinking about? Do you know somebody with a bulldozer? What’s your favorite breed of goat?’”

The Aars recently began keeping honeybees and hope for a honey harvest in late summer 2019. One day, they plan to split hives to sell the bees as well. The farm is also home to goats and a donkey, and Allison wants a cow (Michael says, “We’ll see!”). Ironically, Allison had started a farmhouse-lifestyle business in 2016 prior to the move, and named it “The Festive Farmhouse”. She has created a successful brand and blog that frequently features their home. Now the whole family is living The Festive Farmhouse life!





“We’re watching our kids grow. Their sense of wonder has expanded since we’ve moved here. And so has ours.”

- Michael

A LETTER FROM

OUR INTERIM CEO

You have often heard it said that tough times will either make you or break you. I am proud to report that today's Lone Star Ag Credit remains financially strong and is a much more fiscally responsible institution due to the controls and segregation of duties that have been implemented over the past eighteen months. For the sake of our borrower-owners, employees, and the Ag communities we serve, we made great strides in 2018.

To illustrate Lone Star's financial strength, consider the Association's capital level, asset quality, earnings, liquidity, and efficiency at December 31, 2018:

CAPITAL	19.98%	Permanent Capital Ratio
ASSET QUALITY	98.87%	Acceptable & OAEM
EARNINGS	1.75%	Return on Assets
LIQUIDITY	21.76%	Borrowing Capacity
EFFICIENCY	49.51%	Operating Efficiency

Each of these key performance indicators are indicative of a financially sound institution. In fact, at the end of 2018, Lone Star Ag Credit ranked favorably among the 14 Associations funded by the Farm Credit Bank of Texas.

Another key indicator of Lone Star's robust financial health is the fact that we have been able to pay a record of $20.3 million in patronage on our 2018 earnings. This is the largest distribution in Lone Star's history, and brings the total of earnings returned to our stockholders to $122 million since 2000.

During fiscal year 2019, the Association has two primary objectives: 1) improve the customer experience and 2) pay a significant cash patronage to our stockholders. Plans to achieve these objectives include:

- Evaluating avenues to improve credit delivery to the customer.
- Facilitating quicker approvals on loans through greater usage of automated loan decisioning tools.

- Improving communications with existing borrowers to better understand their complete credit needs.
- Organizing our lending teams to ensure customers have an experienced lender and credit analyst who are knowledgeable of their customer's operations.
- Optimizing use of technology to communicate with customers.

Lone Star is proud to serve our customers and Ag communities across our chartered territory of 48 counties. Our territory includes the fertile producing areas in northeast Texas; farming and ranching land in central Texas; and, at the center of our territory, the Dallas/Fort Worth metroplex, an area where we support significant opportunities for lifestyle or part-time farms, hunting, and recreational tracts.

The future is bright for Lone Star, not only because of where we serve, but because of how we develop relationships with our customers. Here are just a few reasons why customers and prospects choose to do business with Lone Star Ag Credit:

- We provide competitive interest rates and terms.
- We provide excellent customer service and serve as a resource to customers.
- We work with our customers in good times and bad.
- We strive to pay patronage consistently to our stockholders.

From the creation of the Farm Credit System and the first loan made more than 100 years ago by Lone Star, our mission has been to improve the income and financial well-being of our stockholders. Lone Star is truly blessed with a rich agricultural heritage, a passion for farming, and a value for family and faith, common traits among all Farm Credit institutions where I have worked.

We appreciate your business and will do our best to earn it every day, and year after year. May God bless you and your family and, through those blessings, let's commit to being good stewards of all the resources God has committed to our stewardship.

William L. Melton

William L. (Bill) Melton
Interim CEO, Lone Star Ag Credit

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REPORT OF MANAGEMENT

The consolidated financial statements of Lone Star, ACA, including its wholly-owned subsidiaries, Lone Star, PCA and Lone Star, FLCA (collectively referred to as the “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 auditors, who also obtain an understanding of internal controls to the extent necessary to comply 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 (Board) has overall responsibility for the Association’s systems of internal control and financial reporting. The Board consults regularly with management and reviews the results of the audits and examinations referred to previously.

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

William L. (Bill) Melton, Interim Chief Executive Officer

March 13, 2019

David Harris, Chairman, Board of Directors

March 13, 2019

Amy Birt, Chief Financial Officer

March 13, 2019

Don Crawford, Chairman, Audit Committee

March 13, 2019

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

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

The Association's management has completed an assessment of the effectiveness of internal control over financial reporting as of December 31, 2018. 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.

As disclosed in our 2017 Annual Report, management concluded that we had material weaknesses in our internal control over financial reporting. A material weakness is a control deficiency, or a combination of control deficiencies, that results in a more than remote likelihood that a material misstatement of the Association's annual or interim consolidated financial statements will not be prevented or detected on a timely basis. The Association's management concluded that the following material weaknesses existed in the following areas as of December 31, 2017:

- Disbursements – loan disbursements (check and construction draws) were made without proper documentation and approval. Checks could be issued without being complete, accurate and properly recorded due to lack of segregation of duties;
- Cash Control Transfers – policies and procedures related to transfers between loan accounts were not in place, thereby allowing inaccurate entries to the loan accounting system;
- Segregation of Duties – there were ineffective segregation of duties and monitoring processes related to several system accesses in the loan origination and accounting systems, which created the potential for unauthorized activity.

In 2018, the Association remediated the material weaknesses by executing the following:

- Loan disbursements were centralized with approval of disbursements, supported by required supporting documentation and authorized approvals, initiated by our treasury group;
- Access restrictions and user access controls were established whereby authorized accesses to originate and fund loans were limited to the Association's loan operations and treasury groups;
- Segregation of duties related to loan operations were refined whereby the ability to post to the Association's loan accounting systems were restricted to nonlending personnel;
- The Association conducted a thorough review of the lending and accounting processes ensuring personnel have the appropriate training and experience.

Based on our testing of the design and operational effectiveness of our procedures, our management concludes that we have remediated the material weaknesses and as of December 31, 2018 the internal control over financial reporting was effective based upon the COSO criteria. A review of the assessment performed was reported to the Association's Audit Committee.

William L. (Bill) Melton, Interim Chief Executive Officer

March 13, 2019

Amy Birt, Chief Financial Officer

March 13, 2019

REPORT OF AUDIT COMMITTEE

The Audit Committee (Committee) is composed of five members from the board of directors of Lone Star, ACA. Don Crawford, CPA, serves as the chairman of the Committee, and David W. Conrad, CPA, serves as vice chairman. Cody Hughes, Brent Neuhaus and Bert Pruett are also members of the Committee. In 2018, 12 committee meetings were held. The Committee oversees the scope of Lone Star, ACA'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 Lone Star, ACA's website. The Committee approved the appointment of PricewaterhouseCoopers LLP, independent auditors, to perform the consolidated financial statement audit for 2018.

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

In this context, the Committee reviewed and discussed both Lone Star, ACA's audited consolidated financial statements for the year ended December 31, 2018 with management and PricewaterhouseCoopers LLP. The Committee also reviews with PricewaterhouseCoopers LLP the matters required to be discussed by authoritative guidance "The Auditor's Communication With Those Charged With Governance," and both PricewaterhouseCoopers LLP's and Lone Star, ACA's internal auditors directly provide reports on significant matters to the Committee.

The Committee discussed with PricewaterhouseCoopers LLP its independence from Lone Star, ACA. The Committee also reviewed the nonaudit services provided by PricewaterhouseCoopers LLP and concluded that these services were not incompatible with maintaining the independent auditor's independence. The Committee has discussed with management and PricewaterhouseCoopers LLP such other matters and received such assurances from them as the Committee deemed appropriate.

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 Lone Star, ACA's Annual Report to Stockholders for the year ended December 31, 2018.

Audit Committee Members

Don Crawford, CPA
David W. Conrad, CPA
Cody Hughes
Brent Neuhaus
Bert Pruett

March 13, 2019

DISCLOSURE INFORMATION AND INDEX

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 from Note 1 to the consolidated financial statements, "Organization and Operations," included in this annual report.

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

DESCRIPTION OF PROPERTY

Lone Star, ACA serves its 48-county territory through its main administrative and lending office at 1612 Summit Avenue, Suite 300, Fort Worth, Texas 76102. Additionally, there are 15 branch lending offices located throughout the territory. The Association owns the office buildings in Paris, New Boston, Denton, Cleburne, Stephenville, Sweetwater, Lampasas, Corsicana, Hillsboro and Waco. The Association leases office space in Fort Worth, Sherman, Abilene, Weatherford and Georgetown.

LEGAL PROCEEDINGS

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

DESCRIPTION OF CAPITAL STRUCTURE

The information required to be disclosed in this section is incorporated herein by reference from Note 10 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 9, "Note Payable to the Bank," Note 12, "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 15 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 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 Lone Star, ACA 1612 Summit Avenue, Suite 300, Fort Worth, Texas 76102 or calling (817) 332-6565. Copies of the Association's quarterly stockholder reports can also be requested by e-mailing *Tonya.Arvin@lonestaragcredit.com*. The Association's annual stockholder report is available on our website at www.lonestaragcredit.com 75 days after the fiscal year end. Copies of the Association's annual stockholder report can also be requested 90 days after the fiscal year end.

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

	2018	2017	2016	2015	2014
Balance Sheet Data					
Assets					
Cash	**$ 100**	$ 90	$ 61	$ 56	$ 72
Loans	**1,559,619**	1,681,073	1,648,167	1,553,142	1,400,308
Less: allowance for loan losses	**(8,645)**	(9,182)	(10,072)	(6,818)	(5,683)
Net loans	**1,550,974**	1,671,891	1,638,095	1,546,324	1,394,625
Investment in and receivable from the Farm Credit Bank of Texas	**29,603**	28,897	27,559	24,328	23,306
Other property owned, net	**-**	-	-	79	201
Other assets	**13,433**	13,118	13,219	12,329	11,382
Total assets	**$ 1,594,110**	$ 1,713,996	$ 1,678,934	$ 1,583,116	$ 1,429,586
Liabilities					
Obligations with maturities of one year or less	**$ 30,983**	$ 11,862	$ 26,652	$ 24,031	$ 24,158
Obligations with maturities greater than one year	**1,219,700**	1,361,491	1,322,671	1,231,371	1,088,806
Total liabilities	**1,250,683**	1,373,353	1,349,323	1,255,402	1,112,964
Members' Equity					
Capital stock and participation certificates	**5,911**	6,387	6,432	6,339	6,367
Additional paid-in capital	**91,343**	91,343	91,343	91,343	91,343
Allocated retained earnings	**-**	-	-	3,000	7,115
Unallocated retained earnings	**246,572**	244,271	232,669	227,852	213,133
Accumulated other comprehensive income (loss)	**(399)**	(1,358)	(833)	(820)	(1,336)
Total members' equity	**343,427**	340,643	329,611	327,714	316,622
Total liabilities and members' equity	**$ 1,594,110**	$ 1,713,996	$ 1,678,934	$ 1,583,116	$ 1,429,586
Statement of Income Data					
Net interest income	**$ 48,025**	$ 47,043	$ 44,331	$ 43,654	$ 40,943
(Provision for loan losses) or loan loss reversal	**576**	630	(2,821)	(722)	1,080
Income from the Farm Credit Bank of Texas	**6,592**	6,237	6,152	5,724	5,657
Other noninterest income	**2,001**	1,147	821	840	1,045
Noninterest expense	**(27,540)**	(43,468)	(29,767)	(21,884)	(21,695)
Benefit from income taxes	**(24)**	(1)	-	(45)	53
Net income (loss)	**$ 29,630**	$ 11,588	$ 18,716	$ 27,567	$ 27,083
Key Financial Ratios for the Year					
Return on average assets	**1.8%**	0.7%	1.2%	1.8%	1.9%
Return on average members' equity	**8.5%**	3.4%	5.6%	8.4%	8.5%
Net interest income as a percentage of average earning assets	**2.9%**	2.8%	2.7%	3.0%	3.0%
Net charge-offs (recoveries) as a percentage of average loans	**0.0%**	0.0%	0.0%	0.0%	0.0%

LONE STAR, ACA

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

	2018	2017	2016	2015	2014
Key Financial Ratios at Year End *					
Members' equity as a percentage of total assets	**21.5%**	19.9%	19.6%	20.7%	22.1%
Debt as a percentage of members' equity	**364.2%**	403.2%	409.4%	383.1%	351.5%
Allowance for loan losses as a percentage of loans	**0.6%**	0.5%	0.6%	0.4%	0.4%
Common equity tier 1 ratio	**19.9%**	18.0%	n/a	n/a	n/a
Tier 1 capital ratio	**19.9%**	18.0%	n/a	n/a	n/a
Total capital ratio	**20.4%**	18.5%	n/a	n/a	n/a
Permanent capital ratio	**20.0%**	18.1%	18.9%	19.7%	21.4%
Tier 1 leverage ratio	**20.7%**	18.9%	n/a	n/a	n/a
UREE leverage ratio	**22.0%**	20.0%	n/a	n/a	n/a
Core surplus ratio	**n/a**	n/a	18.3%	19.3%	21.0%
Total surplus ratio	**n/a**	n/a	18.5%	19.3%	21.0%
Net Income Distribution					
Cash dividends paid	**$ 7,050**	$ 13,810	$ 15,923	$ 16,221	$ 16,447

* Effective January 1, 2017 the new regulatory capital ratios were implemented by the Association. Regulatory ratios remained well above regulatory minimums, including the conservation and leverage buffers at December 31, 2018.

MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
(Unaudited)

The following commentary explains management's assessment of the principal aspects of the consolidated financial condition and results of operations of Lone Star, ACA, including its wholly-owned subsidiaries, Lone Star, PCA and Lone Star, FLCA (collectively referred to as the "Association") for the years ended December 31, 2018, 2017 and 2016, and should be read in conjunction with the accompanying consolidated financial statements. The accompanying financial statements were prepared under the oversight of the Association's Audit Committee.

Forward-Looking Information:

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

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

Significant Events:

In December 2018, the Board of Lone Star, ACA declared a 150 basis point (1.5 percent) cash patronage to be paid in March of 2019 based on 2018 earnings. The patronage amount to be paid is $20,377,032. The patronage will be paid to eligible borrowers based on their average outstanding loan balance for the year ending December 31, 2018. The Association's total capital position remains strong at 20.0 percent for the period ending December 2018.

In July 2018, the Association's Board of Directors approved to pay a cash patronage of $7,049,954, 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.

In 2017 and 2016, the Association paid a cash patronage of $13,809,745 and $15,923,462, respectively.

The following table provides information on the patronage received from the Bank for the years ended December 31, 2018, 2017 and 2016, respectively:

	2018	2017	2016
Direct loan patronage	**$ 5,518,014**	$ 5,355,288	$ 5,320,436
Special loan patronage	**134,596**	-	-
Stock investment in the Farm Credit Bank of Texas	**729,181**	571,987	453,974
Participation's patronage	**-**	18,615	62,033

The direct loan patronage received in 2018, 2017 and 2016 represents 42, 39 and 41 basis points, respectively, on the average daily balance of the Association's direct loan with the Bank. The participation's patronage received represents 75 basis points on the Association's average balance of participations sold into the Bank's patronage pool program.

On November 7, 2018, the CEO's (Troy Bussmeir) resignation was accepted by the Board and on November 8, 2018 William L. (Bill) Melton was named Interim CEO.

Since 1917, the Association and its predecessors have provided its members with quality financial services. The Board 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.

Loan Portfolio:

The Association makes and services loans to farmers, ranchers, rural homeowners and certain farm-related businesses. The Association's loan volume consists of long-term farm mortgage loans, production and intermediate-term loans, and farm-related business loans. These loan products are available to eligible borrowers with competitive variable, fixed, adjustable, LIBOR-based and prime-based interest rates. Commercial loans primarily consist of operating loans and short-term loans for working capital, equipment and livestock. Mortgage loans primarily consist of 20- to 40- year maturities. Loans serviced by the Association offer several installment payment cycles, the timing of which usually coincides with the seasonal cash-flow capabilities of the borrower.

The composition of the Association's loan portfolio, including principal less funds held of $1,559,619,163, $1,681,072,602 and $1,648,166,522 as of December 31, 2018, 2017 and 2016, respectively, is described more fully in detailed tables in Note 5 to the consolidated financial statements, "Loans and Allowance for Loan Losses" included in this annual report.

Purchase and Sales of Loans:

The following table provides information on participations purchased and sold during the year ended December 31:

	2018	2017	2016
Participations purchased from other:			
Farm credit institutions	**$ 244,014,725**	$ 245,040,983	$ 254,569,519
Farm credit institutions to total loans	**15.6%**	14.6%	15.4%
Entities outside the district	**1,728,704**	1,408,928	975,473
Participations sold	**6,413,551**	9,653,120	26,126,415

Effective January 26, 2012 the Bank purchased Lone Star, ACA's securitized Farmer Mac Agricultural Mortgage Backed Securities (AMBS) Investments. The purchase of $35,459,508 included outstanding principal and accrued interest as of that date. There was no gain or loss recognized by the Association on this transaction. The Association will continue to service the underlying loans that were included in this security. Also, there is intended to be no effect to Lone Star, ACA's income based on this transaction as it is expected that the Bank will be able to pay the Association a patronage equivalent to the net interest that would have been earned on the AMBS investment. However, the Bank's payment of patronage is at the discretion of the Bank's board of directors. The remaining balance of the AMBS investment at December 31, 2018 was $8,600,315.

Risk Exposure:

High-risk assets include nonaccrual loans, loans that are past due 90 days or more and still accruing interest, formally restructured loans and other property owned, net.

The following table illustrates the Association's components and trends of high-risk assets serviced for the prior three years as of December 31:

	2018			2017			2016		
	Amount	**%**	**% Loan Volume**	Amount	%	% Loan Volume	Amount	%	% Loan Volume
Nonaccrual	**$ 4,356,030**	**74.7%**	**0.3%**	$ 5,633,106	55.4%	0.3%	$ 6,207,663	66.7%	0.4%
Formally restructured	**1,474,500**	**25.3%**	**0.1%**	4,537,338	44.6%	0.3%	3,106,032	33.3%	0.2%
Total	**$ 5,830,530**	**100.0%**	**0.4%**	$ 10,170,444	100.0%	0.6%	$ 9,313,695	100.0%	0.6%

During 2018, the Association experienced a $1,277,076 net decrease in nonaccrual loan volume for a total outstanding volume of $4,356,030 as of December 31, 2018. The primary driver of the decrease in nonaccruals from 2017 was loan payoffs totaling $2,546,686. Of the $4,356,030 in nonaccrual at December 31, 2018, beef cattle comprised $2,288,335; cash grains comprised

$668,883; horses and other equines comprised $543,918; field crops comprised $461,049; and rural home comprised $354,236; with the remaining balance of nonaccrual volume being comprised by other various commodities.

During 2018, the Association experienced a $3,062,838 decrease in formally restructured loans for a total outstanding volume of $1,474,500. The decrease was primarily attributed to the payoff of a commercial real estate relationship. The relationship consisted of four loans totaling $2,979,286 at the time of payoff. During 2017 this relationship was moved from nonaccrual to accrual status when the Association refinanced eleven loans into four loans. Originally the loan was downgraded to nonaccrual status due to loan performance. However, it was later discovered that the apparent non-performance was the result of the Borrowers' understanding of the loan terms differing from the terms documented in the loan system due to misinformation supplied by a former loan officer. The Borrowers were performing according to the terms communicated to them. As such, the loans were refinanced consistent with the Borrowers' understanding of the original loan terms, which allowed them to maintain performance under the refinanced terms. Additionally, the refinancing of loans better protected the Association from loss in the event of a future default as the Borrower was able to reduce Association debt levels and the refinanced loans were more favorably structured.

At December 31, 2018 the Association held no property classified as other property owned.

Except for the relationship between installment due date and seasonal cash-flow capabilities 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 Loan Losses:

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

	2018	2017	2016
Allowance for loan losses	**$ 8,645,430**	$ 9,181,997	$ 10,071,747
Allowance for loan losses to total loans	**0.6%**	0.5%	0.6%
Allowance for loan losses to nonaccrual loans	**198.5%**	163.0%	162.2%
Allowance for loan losses to impaired loans	**148.3%**	91.1%	108.1%
Net charge-offs to average loans	**0.0%**	0.0%	0.0%

The allowance is based on a periodic evaluation of the loan portfolio by management in which numerous factors are considered, including economic conditions, loan portfolio composition, collateral value, portfolio quality, current production conditions and economic conditions, and prior loan loss experience. Management may consider other qualitative factors in determining and supporting the level of allowance for loan losses including but not limited to: the concentration of lending in agriculture, combined with uncertainties associated with farmland values, commodity prices, exports, government assistance programs, regional economic effects, borrower repayment capacity, depth of lender staff, and/or past trends, and weather-related influences.

Based upon ongoing risk assessment and the evaluation process for allowance for loan losses outlined above, the allowance for loan losses is considered adequate by management to compensate for inherent losses in the loan portfolio. Management's process for the evaluation of allowance for loan losses includes a portfolio analysis, peer comparison with similar Farm Credit Institutions and similar commercial banks, and an analysis of historical loss experience. As previously noted, the allowance for loan losses increased $3,025,424 for 2016 due to recognition of credit quality deteriorations for loans affected by the events revealed in 2017. The reduction of allowance in 2017 totaling $924,594 reflects the resolution and reassessment of credit quality for a number of these affected loans.

Management utilizes an allowance pool to address the need for additional allowance for under-secured loans, should they deteriorate, and ultimately require a specific allowance. In addition, during 2014 management implemented an additional allowance pool to address the need for allowance for loan commitments that have been established, but are not yet drawn. This allowance pool on unfunded commitments is reflected in other liabilities and is not reflected in the allowance for loan losses balance. In view of portfolio analysis, historical trends, projected needs and the implementation of the additional allowance pool, management believes that the allowance is adequate.

Results of Operations:

The Association's net income for the year ended December 31, 2018 was $30,004,326 as compared to $ 11,587,943 for the year ended December 31, 2017, reflecting an increase of $18,103,109, or 152.1 percent. The Association's net income for the year ended December 31, 2016 was $19,019,402. Net income decreased $7,118,185, or 37.4 percent, in 2017 versus 2016.

Net interest income for 2018, 2017, and 2016 was $48,024,532, $47,042,981, and $44,331,353, respectively, reflecting increases of $981,551, or 2.1 percent, for 2018 versus 2017 and $2,711,628, or 6.1 percent, for 2017 versus 2016. Net interest income is the principal source of earnings for the Association and is impacted by volume, yields on assets and cost of debt. The effects of changes in average volume and interest rates on net interest income over the past three years are presented in the following tables:

	2018		2017		2016	
	Average Balance	**Interest**	Average Balance	Interest	Average Balance	Interest
Loans	**$ 1,635,970,654**	**$ 83,598,040**	$ 1,698,230,836	$ 78,489,105	$ 1,615,659,972	$ 70,890,135
Total interest-earning assets	**1,635,970,654**	**83,598,040**	1,698,230,836	78,489,105	1,615,659,972	70,890,135
Interest-bearing liabilities	**1,307,048,902**	**35,573,508**	1,370,870,127	31,446,124	1,294,961,169	26,558,782
Impact of capital	**$ 328,921,752**		$ 327,360,709		$ 320,698,803	
Net interest income		**$ 48,024,532**		$ 47,042,981		$ 44,331,353

	2018 Average Yield	2017 Average Yield	2016 Average Yield
Yield on loans	**5.11%**	4.62%	4.39%
Total yield on interest-earning assets	**5.11%**	4.62%	4.39%
Cost of interest-bearing liabilities	**2.72%**	2.29%	2.05%
Interest rate spread	**2.39%**	2.33%	2.34%
Net interest income as a percentage of average earning assets	**2.94%**	2.77%	2.74%

	2018 vs. 2017			2017 vs. 2016		
	Increase (decrease) due to			Increase (decrease) due to		
	Volume	**Rate**	**Total**	Volume	Rate	Total
Interest income - loans	**$ (2,877,541)**	**$ 7,986,476**	**$ 5,108,935**	$ 3,622,962	$ 3,976,008	$ 7,598,970
Total interest income	**(2,877,541)**	**7,986,476**	**5,108,935**	3,622,962	3,976,008	7,598,970
Interest expense	**(1,463,995)**	**5,591,379**	**4,127,384**	1,556,817	3,330,525	4,887,342
Net interest income	**$ (1,413,546)**	**$ 2,395,097**	**$ 981,551**	$ 2,066,145	$ 645,483	$ 2,711,628

Interest income for 2018 increased by $5,108,935 or 6.5 percent, compared to 2017, primarily due to increases in yields on earning assets, fair value accretion recognition, and forgone interest recoveries during the year. Interest expense for 2018 increased by $4,127,384, or 13.1 percent, compared to 2017 due to an increase in cost of interest-bearing liabilities, offset by a decrease in average interest-bearing liabilities. The interest rate spread increased by 6 basis points to 2.39 percent in 2018 from 2.33 percent in 2017, as the yield on loans increased on average 0.49 percent during the year while the Association's rate of borrowing from the Bank also increased 0.43 percent.

The Association offers a number of different interest rate programs including fixed rate products lasting for a set period up to the term of a loan, products indexed to Prime or LIBOR, and a variety of adjustable interest rate products. The Association's control over interest rate margins resides in its ability to add a spread over cost of funds, the goal of which is to achieve an acceptable level of income to fund operations and generate a return for shareholders. Net interest margin for year end 2018 was 2.94, versus 2.77 for the same period in 2017.

Noninterest income for 2018 increased by $1,208,235, or 16.4 percent, compared to 2017, due primarily to an increase 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). Additionally, the increase is also attributed to an increase in patronage income from the Bank, which includes $134,596 of special patronage income. Noninterest income for 2017 increased by $411,845, or 5.9 percent, compared to 2016, due primarily to an increase in patronage income from the Bank.

Authoritative accounting guidance requiring the capitalization and amortization of loan origination fees and costs resulted in the capitalization of $1,307,537, $2,515,905, and $2,340,269 for 2018, 2017, and 2016, respectively, in origination fees, and $2,636,198 for 2018 and 2017, and $2,105,609 for 2016 in origination costs, which will be amortized over the life of the loans as an adjustment to yield in net interest income.

Provisions for loan losses increased by $54,424, or 8.6 percent, compared to 2017, due to the Association's adoption of new probability of default percentages during 2018 based on current district industry concentrations and historical data, which are more punitive than the percentages used in 2017. The adoption of the new percentages led to an increase in allowance reserves needed; offset by the decrease of average interest-earning assets.

Operating expenses consist primarily of salaries and employee benefits, purchased services, travel, occupancy and equipment expenses, advertising, public and member relations expenses, and insurance fund premiums. Expenses for purchased services include administrative services, marketing, accounting and loan processing, audit and credit review fees, and legal fees, among others. Net operating expense for 2018, 2017 and 2016 were $27,164,991, $43,155,202, and $29,463,912, respectively, reflecting a decrease of $15,990,211 or 37.1 percent for 2018 and an increase of $13,691,290 or 46.5 percent for 2017.

The decrease in operating expenses for 2018 was driven primarily by a decrease in purchased services and other noninterest expense of $5,781,245 and $10,568,401, respectively, compared to 2017, due mostly to expenses related to the breach of Association policies and procedures by a former loan officer in 2017 with no comparable expenses in 2018.

For the year ended December 31, 2018, the Association's return on average assets was 1.8 percent, as compared to 0.7 percent and 1.1 percent for the years ended December 31, 2017 and 2016, respectively. For the year ended December 31, 2018, the Association's return on average members' equity was 8.5 percent, as compared to 3.3 percent and 5.5 percent for the years ended December 31, 2017 and 2016, respectively.

Liquidity and Funding Sources:

The primary source of liquidity and funding for the Association is a direct loan from the Bank. The outstanding balances of $1,216,709,990, $1,358,683,640, and $1,320,377,658 as of December 31, 2018, 2017, and 2016, respectively, are recorded as a liability on the Association's balance sheet. The note carried a weighted average interest rate of 2.72 percent, 2.29 percent, and 2.05 percent at December 31, 2018, 2017 and 2016, respectively. The indebtedness is collateralized by a pledge of substantially all of the Association's assets to the Bank and is governed by a General Financing Agreement ("GFA"). The decrease in the Association's note payable to the Bank and related accrued interest payable since December 31, 2017 correlates directly with the overall decrease in Association loan volume and increased average cost. The Association's own funds, which represent the amount of the Association's loan portfolio funded by the Association's equity, were $342,111,750, $337,712,474, and $333,586,191 at December 31, 2018, 2017, and 2016, respectively. The maximum amount the Association may borrow from the Bank as of December 31, 2018 was $1,495,465,641 as defined by the GFA. The indebtedness continues in effect until the expiration date of the GFA, which is September 30, 2020, unless terminated sooner 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 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.

Because the Association depends on the Bank for funding, any significant positive or negative factors affecting the operations of the Bank may have an effect on the operations of the Association.

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 2019. As borrower payments are received, they are applied to the Association's note payable to the Bank.

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

Capital Resources:

The Association's capital position remains strong, with total members' equity of $343,427,378, $340,643,552, and $329,610,453 at December 31, 2018, 2017 and 2016, respectively.

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.

Risk-adjusted:	Regulatory Minimums	Conservation Buffer*	Total	As of December 31, 2018
Common equity tier 1 ratio	4.50%	2.50%	7.00%	19.87%
Tier 1 capital ratio	6.00%	2.50%	8.50%	19.87%
Total capital ratio	8.00%	2.50%	10.50%	20.44%
Permanent capital ratio	7.00%	0.00%	7.00%	19.98%
Non-risk-adjusted:				
Tier 1 leverage ratio**	4.00%	1.00%	5.00%	20.68%
UREE leverage ratio	1.50%	0.00%	1.50%	22.04%

*The 2.5% capital conservation buffer for the risk-adjusted ratios will be phased in over a three-year period ending on December 31, 2019. There is no phase-in of the leverage buffer.

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

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, 2018, 2017 and 2016 was 20.0 percent, 18.1 percent and 18.9 percent, respectively.

The Association's members' equity includes accumulated other comprehensive loss (AOCL) related to certain health care benefits to qualifying retired employees (other postretirement benefits). These benefits are not characterized as multi-employer and, consequently, the liability for these benefits is included in other liabilities. The AOCL includes net actuarial losses and prior service costs/credits that have been included in liabilities, but have not yet been amortized into earnings.

In 2018, 2017 and 2016, the Association paid patronage of $7,049,954, $13,809,745 and $15,923,462, respectively.

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. The Association early adopted the removal and modified disclosures during the fourth quarter of 2018.

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 percent to 21 percent. 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 evaluated the guidance and there is no impact 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 adoption of this guidance will not impact the Association's financial condition or 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 will 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 became effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance will not impact the Association's financial condition or its results of operations.

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 the Association's financial condition and its results of operations.

In February 2016, the FASB issued guidance entitled "Leases." The guidance requires the recognition by lessees of lease assets and lease liabilities on the balance sheet for the rights and obligations created by those leases. Leases with lease terms of more than 12 months are impacted by this guidance. 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 updated disclosure become effective for interim and annual periods beginning after December 15, 2018, with early application permitted. Based on the Association's analysis, the impact of the new lease accounting standard will result in recording a Right of Use Asset and Lease Liability of $1,488,212 with an immaterial impact to results of operations, and no impact on the Association's statement of cash flows.

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 became 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 Farm Credit Administration (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 July 28, 2016, the Farm Credit Administration published a final regulation to modify the regulatory capital requirements for System banks and associations. The stated objectives of the proposed rule were 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 final rule replaces existing core surplus and total surplus requirements with common equity tier 1, tier 1 and total capital risk-based capital ratio requirements. The final rule also replaces the existing net collateral ratio with a tier 1 leverage ratio and is applicable to all banks and associations. The permanent capital ratio will continue to remain in effect with the final rule.

The new capital requirements became effective January 1, 2017, with a three-year phase-in of the capital conservation buffer applied to the risk-adjusted capital ratios. The Association is in compliance with the required minimum capital standards and met the conservation buffers as of December 31, 2018.

On June 12, 2014, the Farm Credit Administration approved a proposed rule to revise the requirements governing the eligibility of investments for System banks and associations. The stated objectives of the proposed rule are as follows:

- To strengthen the safety and soundness of System banks and associations,
- To ensure that System banks hold sufficient liquidity to continue operations and pay maturing obligations in the event of market disruption,
- To enhance the ability of the System banks to supply credit to agricultural and aquatic producers,
- To comply with the requirements of section 939A of the Dodd-Frank Act,

- To modernize the investment eligibility criteria for System banks and
- To revise the investment regulation for System associations to improve their investment management practices so they are more resilient to risk.

FCA released the final ruling in the first quarter of 2019. The ruling has no impact on the Association.

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 capital of the Association is discussed in Note 2 to the consolidated financial statements, "Summary of Significant Accounting Policies," included in this annual report, within the section "Capital Stock Investment in the Farm Credit Bank of Texas."

The Bank's role in mitigating the Association's exposure to interest rate risk is described in the section "Liquidity and Funding Sources" of Management's Discussion and Analysis and in Note 9 to the consolidated financial statements, "Note Payable to the Bank," included in this annual report.

The Bank provides computer systems to support the critical operations of all district Associations. In addition, each Association has operating systems and facility-based systems that are not supported by the Bank. As disclosed in Note 13 to the consolidated financial statements, "Related Party Transactions," included in this annual report, the Bank provides several services utilized by the Association, such as administrative, marketing, information systems and accounting services. For these services and other allocated expenses, the Bank bills district expenses to the Association.

Summary:

Over the past 100 years, regardless of the state of the agricultural economy, Lone Star and the Bank have been committed to offering their borrowers a ready source of financing at a competitive price. Your continued support will be critical to the success of Lone Star Ag Credit.

pwc

Report of Independent Auditors

To the Board of Directors of Lone Star, ACA

We have audited the accompanying consolidated financial statements of Lone Star, ACA and its subsidiaries, which comprise the consolidated balance sheets as of December 31, 2018, December 31, 2017 and December 31, 2016, and the related consolidated statements of comprehensive income, changes in members' equity and cash flows for the years then ended.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Lone Star, ACA and its subsidiaries as of December 31, 2018, December 31, 2017 and December 31, 2016, 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.

PricewaterhouseCoopers LLP

March 13, 2019

LONE STAR, ACA

CONSOLIDATED BALANCE SHEET

	December 31,		
	2018	2017	2016
Assets			
Cash	**$ 100,291**	$ 90,437	$ 60,478
Loans	**1,559,619,163**	1,681,072,602	1,648,166,522
Less: allowance for loan losses	**(8,645,430)**	(9,181,997)	(10,071,747)
Net loans	**1,550,973,733**	1,671,890,605	1,638,094,775
Accrued interest receivable	**8,983,739**	9,321,322	9,169,528
Investment in and receivable from the Farm Credit Bank of Texas:			
Capital stock	**26,555,545**	27,562,030	26,002,180
Other	**3,047,429**	1,334,685	1,556,926
Premises and equipment	**3,088,636**	2,835,580	3,160,358
Other assets	**1,360,525**	961,471	889,148
Total assets	**$ 1,594,109,898**	$ 1,713,996,130	$ 1,678,933,393
Liabilities			
Note payable to the Farm Credit Bank of Texas	**$ 1,216,709,990**	$ 1,358,683,640	$ 1,320,377,658
Accrued interest payable	**2,990,229**	2,807,131	2,293,082
Drafts outstanding	**76,843**	137,903	229,275
Patronage dividends payable	**20,278,837**	-	13,824,603
Other liabilities	**10,626,621**	11,723,904	12,598,322
Total liabilities	**1,250,682,520**	1,373,352,578	1,349,322,940
Members' Equity			
Capital stock and participation certificates	**5,911,140**	6,386,865	6,431,805
Additional paid-in capital	**91,343,553**	91,343,553	91,343,553
Unallocated retained earnings	**246,571,786**	244,270,903	232,668,103
Accumulated other comprehensive loss	**(399,101)**	(1,357,769)	(833,008)
Total members' equity	**343,427,378**	340,643,552	329,610,453
Total liabilities and members' equity	**$ 1,594,109,898**	$ 1,713,996,130	$ 1,678,933,393

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

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Year Ended December 31, 2018	2017	2016
Interest Income			
Loans	**$ 83,598,040**	$ 78,489,105	$ 70,890,135
Total interest income	**83,598,040**	78,489,105	70,890,135
Interest Expense			
Note payable to the Farm Credit Bank of Texas	**35,572,894**	31,446,079	26,558,764
Advance conditional payments	**614**	45	18
Total interest expense	**35,573,508**	31,446,124	26,558,782
Net interest income	**48,024,532**	47,042,981	44,331,353
(Loan loss reversal) provision for loan losses	**(575,719)**	(630,143)	2,820,657
Net interest income after provision for losses	**48,600,251**	47,673,124	41,510,696
Noninterest Income			
Income from the Farm Credit Bank of Texas:			
Patronage income	**6,591,895**	6,237,662	6,151,906
Loan fees	**322,658**	325,471	481,259
Financially related services income	**7,572**	9,018	11,689
Gain on other property owned, net	**23,723**	92,948	76,180
Gain (loss) on sale of premises and equipment, net	**365,828**	369,649	(4,298)
Other noninterest income	**1,280,998**	349,691	255,858
Total noninterest income	**8,592,674**	7,384,439	6,972,594
Noninterest Expenses			
Salaries and employee benefits	**13,293,787**	11,444,518	14,482,137
Other components of net periodic postretirement benefit cost	**374,652**	313,274	303,165
Directors' expense	**477,011**	462,176	471,429
Purchased services	**6,552,682**	12,333,927	1,354,265
Travel	**1,007,798**	1,279,488	865,946
Occupancy and equipment	**1,447,140**	1,363,924	1,456,512
Communications	**375,791**	327,971	347,228
Advertising	**634,506**	882,206	936,177
Public and member relations	**956,321**	1,242,430	1,143,980
Supervisory and exam expense	**627,966**	408,114	484,476
Insurance Fund premiums	**1,084,996**	2,135,054	2,268,342
Other noninterest expense	**706,993**	11,275,394	5,653,420
Total noninterest expenses	**27,539,643**	43,468,476	29,767,077
Income before income taxes	**29,653,282**	11,589,087	18,716,213
Provision for (benefit from) income taxes	**23,608**	1,144	(24)
NET INCOME	**29,629,674**	11,587,943	18,716,237
Other comprehensive income:			
Change in postretirement benefit plans	**958,668**	(524,761)	(12,261)
Other comprehensive income, net of tax	**958,668**	(524,761)	(12,261)
COMPREHENSIVE INCOME	**$ 30,588,342**	$ 11,063,182	$ 18,703,976

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

LONE STAR, ACA

CONSOLIDATED STATEMENT OF CHANGES IN MEMBERS' EQUITY

	Capital Stock/ Participation Certificates	Additional Paid-in-Capital	Retained Earnings Allocated	Retained Earnings Unallocated	Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
Balance at December 31, 2015	$ 6,339,120	$ 91,343,553	$ 3,000,029	$ 227,852,221	$ (820,747)	$ 327,714,176
Comprehensive income	-	-	-	18,716,237	(12,261)	18,703,976
Capital stock/participation certificates and allocated retained earnings issued	891,385	-	-	-	-	891,385
Capital stock/participation certificates and allocated retained earnings retired	(798,700)	-	-	-	-	(798,700)
Dividends declared	-	-	-	(13,900,355)	-	(13,900,355)
Patronage dividends:						
Capital stock/participation certificates and allocated retained earnings	-	-	(3,000,029)	-	-	(3,000,029)
Balance at December 31, 2016	6,431,805	91,343,553	-	232,668,103	(833,008)	329,610,453
Comprehensive income	-	-	-	11,587,943	(524,761)	11,063,182
Capital stock/participation certificates issued	766,785	-	-	-	-	766,785
Capital stock/participation certificates and allocated retained earnings retired	(811,725)	-	-	-	-	(811,725)
Dividends adjustments	-	-	-	14,857	-	14,857
Balance at December 31, 2017	6,386,865	91,343,553	-	244,270,903	(1,357,769)	340,643,552
Comprehensive income	-	-	-	29,629,674	958,668	30,588,342
Capital stock/participation certificates issued	394,630	-	-	-	-	394,630
Capital stock/participation certificates and allocated retained earnings retired	(870,355)	-	-	-	-	(870,355)
Dividends declared	-	-	-	(27,328,791)	-	(27,328,791)
Balance at December 31, 2018	**$ 5,911,140**	**$ 91,343,553**	**$ -**	**$ 246,571,786**	**$ (399,101)**	**$ 343,427,378**

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

LONE STAR, ACA

CONSOLIDATED STATEMENT OF CASH FLOWS

	Year Ended December 31,		
	2018	2017	2016
Cash flows from operating activities:			
Net income	**$ 29,629,674**	$ 11,587,943	$ 18,716,237
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses (loan loss reversal)	**(575,719)**	(630,143)	2,820,657
Net change in fair value of concessions granted	**864,813**	12,483,286	2,141,609
Gain on sale of other property owned, net	**(23,723)**	(92,949)	(76,180)
Depreciation and amortization	**1,140,181**	1,312,083	982,164
Amortization (accretion) of net (premiums) discounts in investments	**(213,593)**	(246,981)	(246,981)
(Gain) loss on sale of premises and equipment, net	**(365,828)**	(369,649)	4,298
Decrease (increase) in accrued interest receivable	**337,583**	(151,794)	(747,248)
(Increase) decrease in other receivables from the Farm Credit Bank of Texas	**(1,712,744)**	222,241	(509,675)
Increase in other assets	**(399,054)**	(72,323)	(64,318)
Increase in accrued interest payable	**183,098**	514,049	265,562
Increase (decrease) in other liabilities	**2,589**	(1,511,527)	1,575,431
Net cash provided by operating activities	**28,867,277**	23,044,236	24,861,556
Cash flows from investing activities:			
Decrease (increase) in loans, net	**120,163,830**	(45,691,722)	(96,548,313)
Cash recoveries of loans previously charged off	**691,154**	692,795	515,367
Proceeds from redemption (purchase) of invesment in the Farm Credit Bank of Texas	**1,006,485**	(1,559,850)	(2,721,400)
Purchases of premises and equipment	**(1,030,403)**	(767,451)	(927,229)
Proceeds from sales of premises and equipment	**439,538**	392,626	88,690
Proceeds from sales of other property owned	**26,318**	153,356	116,911
Net cash provided by (used in) investing activities	**$ 121,296,922**	$ (46,780,246)	$ (99,475,974)

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

LONE STAR, ACA

CONSOLIDATED STATEMENT OF CASH FLOWS

	Year Ended December 31,		
	2018	2017	2016
Cash flows from financing activities:			
Net (repayment of) draws on note payable to the Farm Credit Bank of Texas	**$ (142,567,606)**	$ 37,712,026	$ 90,440,179
(Decrease) increase in drafts outstanding	**(61,060)**	(91,372)	9,796
Issuance of capital stock and participation certificates	**394,630**	766,785	891,385
Retirement of capital stock and participation certificates	**(870,355)**	(811,725)	(798,700)
Cash dividends paid	**(7,049,954)**	(13,809,745)	(15,923,462)
Net cash (used in) provided by financing activities	**(150,154,345)**	23,765,969	74,619,198
Net increase in cash	**9,854**	29,959	4,780
Cash at the beginning of the year	**90,437**	60,478	55,698
Cash at the end of the year	**$ 100,291**	$ 90,437	$ 60,478
Supplemental schedule of noncash investing and financing activities:			
Loans transferred to other property owned	**$ -**	$ 59,904	$ 39,885
Loans charged off	**793,206**	1,140,054	34,534
Undocumented advances expensed, net	**-**	(2,558,177)	2,858,177
Patronage dividends declared	**27,328,791**	-	13,824,603
Transfer of allowance for loan losses from (into) reserve for unfunded commitments	**141,204**	(112,348)	(47,164)
Supplemental cash information:			
Cash paid during the year for:			
Interest	**$ 35,390,410**	$ 30,932,075	$ 25,964,807

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

LONE STAR, ACA
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 — ORGANIZATION AND OPERATIONS:

A. Organization: Lone Star, ACA, including its wholly-owned subsidiaries, Lone Star, PCA and Lone Star, FLCA (collectively called "the Association"), is a member-owned cooperative which provides credit and credit-related services to, or for the benefit of, eligible borrowers/stockholders for qualified agricultural purposes in the 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, Somerville, 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 (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, 2017, the System consisted of three Farm Credit Banks (FCBs) and their affiliated Associations, one Agricultural Credit Bank (ACB) and its affiliated Associations, the Federal Farm Credit Banks Funding Corporation (Funding Corporation) and various service and other organizations.

The Farm Credit Bank of Texas (Bank) and its related Associations are collectively referred to as the "District." The Bank provides funding to all Associations within the district and is responsible for supervising certain activities of the district Associations. At December 31, 2018, the District consisted of the Bank, one FLCA and 13 ACA parent companies, which have two wholly-owned subsidiaries, an FLCA and a PCA, operating in or servicing the states of Alabama, Louisiana, Mississippi, New Mexico and Texas. ACA parent companies provide financing and related services through their FLCA and PCA subsidiaries. The FLCA makes secured long-term agricultural real estate and rural home mortgage loans. The PCA makes short- and intermediate-term loans for agricultural production or operating purposes.

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

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

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.

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 provides a service facilitating the origination of residential loans that are funded by other lenders as well as acting as an intermediary in offering credit life 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 Bank's Annual Report to Stockholders.

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

NOTE 2 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

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

A. Recently Issued or Adopted 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. The Association is evaluating the impact of adoption on the Association's financial condition and its results of operations.

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 percent to 21 percent. 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 evaluated the guidance and there is no impact 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 adoption of this guidance will not impact the Association's financial condition or 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 will 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 became effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance will not impact the Association's financial condition or its results of operations.

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 the Association's financial condition and its results of operations.

In February 2016, the FASB issued guidance entitled "Leases." The guidance requires the recognition by lessees of lease assets and lease liabilities on the balance sheet for the rights and obligations created by those leases. Leases with lease terms of more than 12 months are impacted by this guidance. 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 updated disclosure become effective for interim and annual periods beginning after December 15, 2018, with early application permitted. Based on the Association's analysis, the impact of the new lease accounting standard will result in recording a Right of Use Asset and Lease Liability of $1,488,212 with an immaterial impact to results of operations, and no impact on the Association's statement of cash flows.

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 became 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.

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

C. Loans and Allowance for Loan Losses: Long-term real estate mortgage loans generally have original maturities ranging from five to 40 years. Substantially all short- and intermediate-term loans 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 net deferred loan fees or costs. Interest on loans is accrued and credited to interest income based upon the daily principal amount outstanding. Authoritative accounting guidance requires loan origination fees and direct loan origination costs, if material, to be capitalized and the net fee or cost to be amortized over the life of the related loan as an adjustment to yield. The guidance resulted in the capitalization of $1,307,537, $2,515,905 and $2,340,269 for 2018, 2017 and 2016, respectively, in origination fees and $2,636,198 for 2018 and 2017 and $2,105,609 for 2016 in origination costs, primarily salaries and benefits related to the origination of loans.

The Association has recorded amounts related to the fair value of concessions granted for certain loans related to the breach of Association policies in 2016 and 2017. The concessions granted were either through the refinancing of a relationship or as a result of acceptance of rates and terms previously negotiated, which were more favorable than market terms and rates. The fair value of the concessions is based on the expected future cash flows under the new contractual terms, discounted at a market interest rate. Concession rates and market rates ranged from 1.25% to 5.25% and 3.70% to 6.95%, respectively. The fair value of the concessions are amortized into interest income over the contractual life of the related loans. The unpaid principal balance of loans with discounts for the fair value of concessions granted were $69,688,230, $72,205,060 and $9,605,594 as of December 31, 2018, 2017 and 2016, respectively. The unaccreted fair value of concessions at December 31, 2018, 2017 and 2016 were $13,760,082, $14,624,894 and $2,141,609, respectively. Amounts accreted into interest income for the years ended December 31, 2018, 2017 and 2016 were $864,813, $181,820 and $13,279, respectively.

Loans acquired in a business combination are initially recognized at fair value, and therefore, no "carryover" of the allowance for loan losses is permitted. Those loans with evidence of credit quality deterioration at purchase are required to follow the authoritative accounting guidance on "Accounting for Certain Loans or Debt Securities Acquired in a Transfer." This guidance addresses accounting for differences between contractual cash flows and cash flows expected to be collected from the initial investment in loans if those differences are attributable, at least in part, to credit quality. The initial fair values for these types of loans are determined by discounting both principal and interest cash flows expected to be collected using an observable discount rate for similar instruments with adjustments that management believes a market participant would consider in determining fair value. Subsequent decreases to expected principal cash flows will result in a charge to the provision for loan losses and a corresponding increase to allowance for loan losses. Subsequent increases in expected principal cash flows will result in recovery of any previously recorded allowance for loan losses, to the extent applicable, and a reclassification from nonaccretable difference to accretable yield for any remaining increase. For variable rate loans, expected future cash flows were initially based on the rate in effect at acquisition; expected future cash flows are recalculated as rates change over the lives of the loans.

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

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

A restructured loan constitutes a troubled debt restructuring (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, there are no unrecovered prior charge-offs and collection of future payments is no longer in doubt. If previously unrecognized interest income exists at the time the loan is transferred to accrual status, cash received at the time of or subsequent to the transfer is first recorded as interest income until such time as the recorded balance equals the contractual indebtedness of the borrower.

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

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

The credit risk-rating methodology is a key component of the Association's allowance for loan losses evaluation, and is generally incorporated into its loan underwriting standards and internal lending limit. The allowance for the loan losses is maintained at a level considered adequate by management to provide for probable losses inherent in the loan portfolio.

The allowance is based on a periodic evaluation of the loan portfolio by management in which numerous factors are considered, including agricultural economy, loan portfolio composition, collateral value, management's process for classification of risk of the loans within the portfolio and the portfolio's prior loss experience. The allowance for loan losses encompasses various judgments, evaluations and appraisals with respect to the loans and their underlying security that, by their nature, contain elements of uncertainty and imprecision. Changes in the agricultural economy and their impact on borrower repayment capacity will cause these various judgments, evaluations and appraisals to change over time. Accordingly, actual circumstances could vary significantly from the institutions' expectations and predictions of those circumstances. The allowance for loan losses process is supported by loan portfolio stress testing, which simulates stress in the current portfolio and the correlating allowance that would be needed.

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

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 ASC 860 "Transfers and Servicing."

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

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

E. 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 loan 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.

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

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

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

   Participants in the DC plan generally include employees who elected to transfer from the DB plan prior to January 1, 1996, and employees hired on or after January 1, 1996. Participants in the DC plan direct the placement of their employers' contributions, 5.0 percent of eligible pay for the years ended December 31, 2018, 2017 and 2016, respectively, made on their behalf into various investment alternatives.

   The structure of the district's DB plan is characterized as multi-employer, since neither the assets, liabilities nor costs of the plan are segregated or separately accounted for by the Associations. No portion of any surplus assets is available to the Associations, nor are the Associations required to pay for plan liabilities upon withdrawal from the plans. As a result, the Associations recognize as pension cost the required contribution to the plans for the year. Contributions due and unpaid are recognized as a liability. The Association recognized pension costs for the DC plan of $470,194, $561,602, and $513,843 for the years ended December 31, 2018, 2017 and 2016, respectively. For the DB plan, the Association recognized pension costs of $744,934, $1,156,528 and $625,890 for the years ended December 31, 2018, 2017 and 2016, 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 $362,062, $464,538 and $440,950 for the years ended December 31, 2018, 2017 and 2016, 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 multi-employer and, consequently, the liability for these benefits is included in other liabilities. In 2004, the District discontinued its multi-employer health and welfare plan, which provided substantially all employees with health care, life insurance and postretirement benefits during their working lives and after retirement if they reach a normal retirement age and met the years of service criteria while working for the Association. At that time, the Association adopted a new plan to provide the same benefits to its retirees and employees. Under the new plan, the Association no longer participates in the joint and several liability with any other entities, which was intrinsic to the multi-employer plan. For employers providing these benefits outside of a multi-employer plan, FASB guidance, "Employers Accounting for Postretirement Benefits Other than Pensions," requires the liability for the contractual obligation of these benefits to be recognized as employees render the services necessary to earn the benefits. Accordingly, in December 2004, the Association recognized as an expense the unfunded liability for these postretirement benefits. Since that time, the net periodic expense for these benefits has been accrued in accordance with this guidance.

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

New U.S. tax laws resulting from legislation commonly known as the Tax Cuts and Jobs Acts of 2017 (TCJA) were enacted in late 2017. Among other things, the TCJA changed the federal corporate tax rate from 35 percent to 21 percent. FLCA subsidiaries are exempt from federal and state income tax; however, the change in the federal corporate tax rate had a financial statement impact for year-end 2017 on ACAs and PCA subsidiaries that required the revaluation of any deferred taxes (assets or liabilities) in the year of enactment (2017). This resulted in a tax expense to the consolidated income statement.

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

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

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

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

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

The fair value disclosures are presented in Note 14, "Fair Value Measurements."

L. Off-balance-sheet credit exposures: Commitments to extend credit are agreements to lend to customers, generally having fixed expiration dates or other termination clauses that may require payment of a fee. Commercial letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. These letters of credit are issued to facilitate commerce and typically result in the commitment being funded when the underlying transaction is consummated between the customer and third party. The credit risk associated with commitments to extend credit and commercial letters of credit is essentially the same as that involved with extending loans to customers and is subject to normal credit policies. Collateral may be obtained based on management's assessment of the customer's creditworthiness. The Association's exposure in off balance-sheet credit exposures is further disclosed in Note 15 "Commitments and Contingencies."

NOTE 3 — INVESTMENTS:

The Association may hold mission-related and other investments. The Farm Credit Administration approves mission-related programs and other mission-related investments. The following is a summary of mission-related and other investments that are held to maturity:

During 2010, the Association exchanged loans totaling $59,626,146 for Federal Agricultural Mortgage Corporation (Farmer Mac) guaranteed mortgage-backed securities (AMBS). The loans were previously covered under the Long-Term Standby Commitment to Purchase Agreements with Farmer Mac. No gain or loss was recognized in the financial statements upon completion of the exchange transactions.

Effective January 26, 2012, the Bank purchased Lone Star's securitized Farmer Mac Agricultural Mortgage Backed Securities (AMBS) Investments. The purchase of $35,459,508 included outstanding principal and accrued interest as of that date. There was no gain or loss recognized by the Association on this transaction. The Association will continue to service the underlying loans that were included in this security. Also, for 2012 there was no effect to Lone Star's income based on this transaction as the Bank was able to pay the Association a patronage equivalent to the net interest that it would have earned on the AMBS investment. The amount of patronage received in 2018, 2017 and 2016 was $210,104, $291,772 and $315,464, respectively. However, for future years, the Bank's payment of patronage is at the discretion of the Bank's board of directors. The remaining balance of the AMBS investment at December 31, 2018 was $8,600,315.

NOTE 4 — LOANS AND ALLOWANCE FOR LOAN LOSSES:

A summary of loans as of December 31 follows:

	2018		2017		2016	
Loan Type	**Amount**	**%**	Amount	%	Amount	%
Real estate mortgage	**$ 1,252,662,987**	**80.3%**	$1,349,434,350	80.4%	$1,298,984,481	78.8%
Production and intermediate term	**93,568,833**	**6.0%**	106,690,588	6.3%	128,286,514	7.8%
Agribusiness:						
Loans to cooperatives	**8,732,264**	**0.6%**	14,281,948	0.8%	14,557,951	0.9%
Processing and marketing	**130,123,023**	**8.3%**	127,788,252	7.6%	117,989,550	7.2%
Farm-related business	**12,730,535**	**0.8%**	15,113,769	0.9%	13,514,114	0.8%
Communication	**8,957,584**	**0.6%**	8,729,168	0.5%	8,068,303	0.5%
Energy	**37,724,209**	**2.4%**	41,992,131	2.5%	45,294,868	2.7%
Water and waste water	**4,947,208**	**0.3%**	3,357,911	0.2%	6,398,890	0.4%
Rural residential real estate	**10,172,520**	**0.7%**	13,684,485	0.8%	15,071,851	0.9%
Total	**$ 1,559,619,163**	**100.0%**	$1,681,072,602	100.0%	$1,648,166,522	100.0%

The Association may purchase or sell participation interests with other parties in order to diversify risk, manage loan volume and comply with Farm Credit Administration regulations. The following table presents information regarding participations purchased and sold as of December 31, 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	$ 16,402,696	$ 6,413,551	$ -	$ -	$ 16,402,696	$ 6,413,551
Production and intermediate term	40,367,606	-	-	-	40,367,606	-
Agribusiness	137,344,126	-	-	-	137,344,126	-
Communication	8,957,584	-	-	-	8,957,584	-
Energy	37,724,209	-	-	-	37,724,209	-
Water and waste water	3,218,504	-	1,728,704	-	4,947,208	-
Total	$ 244,014,725	$ 6,413,551	$ 1,728,704	$ -	$ 245,743,429	$ 6,413,551

Loan volume by office or geographic location as of December 31 follows:

Branch	**2018**	2017	2016
Capital Markets	**15.4%**	14.3%	14.6%
Waco	**11.1%**	11.4%	11.1%
Denton	**10.6%**	9.4%	8.4%
Sherman	**8.1%**	10.0%	16.6%
Stephenville	**6.8%**	7.5%	8.4%
Georgetown*	**6.2%**	6.4%	6.5%
Lampasas	**5.8%**	5.2%	5.0%
Fort Worth	**5.0%**	2.2%	1.5%
Paris	**4.3%**	3.4%	3.9%
Cleburne	**4.2%**	4.5%	4.6%
New Boston	**4.0%**	4.2%	4.4%
Corsicana	**3.9%**	3.8%	3.8%
Special Assets**	**3.9%**	7.2%	0.0%
Abilene	**3.7%**	3.9%	3.9%
Hillsboro	**3.1%**	3.1%	3.4%
Sweetwater	**1.8%**	1.6%	1.7%
Weatherford	**1.7%**	1.6%	1.3%
Participations Purchased	**0.4%**	0.3%	0.9%
Totals	**100.0%**	100.0%	100.0%

*Georgetown opened in 2017 and reflects the Association's Temple and Round Rock branches for 2016, which were closed and consolidated into Georgetown.

** The Special Assets branch was created in 2017 to allow for enhanced monitoring of loans potentially impacted by the breach of Association policies in 2016 and 2017 by a former loan officer. In 2018, only loans impacted by the breach remained in Special Assets as all other loans were moved out to other branches.

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

	2018		2017		2016	
Operation/Commodity	**Amount**	**%**	Amount	%	Amount	%
Livestock, except dairy and poultry	**$ 993,123,008**	**63.7%**	$ 1,101,048,462	65.3%	$ 1,076,010,202	65.2%
Hunting, trapping and game propagation	**83,201,221**	**5.3%**	82,129,518	4.9%	81,984,893	5.0%
General farms, primarily crops	**82,006,021**	**5.3%**	85,575,058	5.1%	73,502,904	4.5%
Field crops except cash grains	**52,928,408**	**3.4%**	50,141,634	3.0%	51,883,595	3.1%
Wholesale trade - nondurable goods	**49,353,148**	**3.2%**	46,124,943	2.7%	42,285,626	2.6%
Timber	**47,795,984**	**3.1%**	41,205,011	2.5%	46,902,035	2.8%
Food and kindred products	**46,732,932**	**3.0%**	54,761,360	3.3%	51,321,395	3.1%
Electric services	**41,136,376**	**2.6%**	43,539,326	2.6%	49,402,615	3.0%
Cash grains	**40,720,965**	**2.6%**	36,402,506	2.2%	39,873,707	2.4%
Animal specialties	**39,497,754**	**2.5%**	40,759,563	2.4%	34,778,819	2.1%
Other	**17,362,597**	**1.1%**	7,885,029	0.5%	12,554,858	0.8%
Paper and allied products	**14,724,880**	**0.9%**	21,218,202	1.3%	24,461,913	1.5%
Rural home loans	**11,035,676**	**0.7%**	14,781,720	0.9%	16,158,786	1.0%
Chemical and allied products	**9,991,243**	**0.6%**	11,810,966	0.7%	4,365,662	0.3%
Farm and garden machinery equipment	**7,401,983**	**0.5%**	9,004,305	0.5%	6,941,461	0.4%
Agricultural services	**6,409,673**	**0.4%**	6,528,539	0.4%	6,220,609	0.4%
Dairy farms	**5,691,642**	**0.4%**	8,807,249	0.5%	10,041,091	0.6%
Fruit and tree nuts	**3,217,221**	**0.2%**	2,649,676	0.2%	2,449,647	0.1%
Poultry and eggs	**2,535,563**	**0.2%**	2,818,637	0.2%	3,066,838	0.2%
Horticultural specialties	**2,180,113**	**0.1%**	2,394,123	0.1%	3,627,955	0.2%
Real estate	**1,512,266**	**0.1%**	1,570,653	0.1%	1,186,164	0.1%
General farms, primarily livestock	**857,630**	**0.1%**	1,065,704	0.1%	917,629	0.1%
Fish hatcheries and preserves	**106,197**	**0.0%**	121,245	0.0%	131,620	0.0%
Public warehousing and storage	**96,662**	**0.0%**	5	0.0%	-	0.0%
Communication	**-**	**0.0%**	8,729,168	0.5%	8,068,303	0.5%
Vegetables and melons	**-**	**0.0%**	-	0.0%	28,195	0.0%
Total	**$ 1,559,619,163**	**100.0%**	$ 1,681,072,602	100.0%	$ 1,648,166,522	100.0%

The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies but typically includes farmland and income-producing property, such as crops and livestock, as well as receivables. Long-term real estate loans are secured by the first liens on the underlying real property. Federal regulations state that long-term real estate loans are not to exceed 85 percent (or 97 percent if guaranteed by a government agency) of the property's appraised value. However, a decline in a property's market value subsequent to loan origination or advances, or other actions necessary to protect the financial interest of the Association in the collateral, may result in 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, 2018, 2017 and 2016, loans totaling $394,135, $436,232 and $480,178, respectively, were guaranteed by these commitments. Fees paid for these guarantees totaled $1,341, $1,483 and $1,624 in 2018, 2017 and 2016, respectively, and are included in "other noninterest expense."

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

	December 31, 2018	December 31, 2017	December 31, 2016
Nonaccrual loans:			
Real estate mortgage	**$ 4,156,191**	$ 3,893,283	$ 3,202,364
Production and intermediate term	**47,546**	1,511,642	2,117,316
Rural residential real estate	**152,293**	228,181	887,983
Total nonaccrual loans	**4,356,030**	5,633,106	6,207,663
Accruing restructured loans:			
Real estate mortgage	**109,118**	3,078,911	3,106,032
Production and intermediate term	**1,365,382**	1,458,427	-
Total accruing restructured loans	**1,474,500**	4,537,338	3,106,032
Total nonperforming loans	**5,830,530**	10,170,444	9,313,695
Total nonperforming assets	**$ 5,830,530**	$ 10,170,444	$ 9,313,695

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

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

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

	2018	2017	2016
Real estate mortgage			
Acceptable	**95%**	95%	94%
OAEM	**4%**	4%	3%
Substandard/doubtful	**1%**	1%	3%
	100%	100%	100%
Production and intermediate term			
Acceptable	**93%**	86%	85%
OAEM	**6%**	11%	5%
Substandard/doubtful	**1%**	3%	10%
	100%	100%	100%
Loans to cooperatives			
Acceptable	**100%**	100%	100%
OAEM	**0%**	0%	0%
Substandard/doubtful	**0%**	0%	0%
	100%	100%	100%
Processing and marketing			
Acceptable	**100%**	100%	97%
OAEM	**0%**	0%	3%
Substandard/doubtful	**0%**	0%	0%
	100%	100%	100%
Farm-related business			
Acceptable	**99%**	93%	93%
OAEM	**0%**	0%	0%
Substandard/doubtful	**1%**	7%	7%
	100%	100%	100%
Communication			
Acceptable	**100%**	100%	100%
OAEM	**0%**	0%	0%
Substandard/doubtful	**0%**	0%	0%
	100%	100%	100%
Energy			
Acceptable	**98%**	98%	98%
OAEM	**2%**	2%	2%
Substandard/doubtful	**0%**	0%	0%
	100%	100%	100%
Water and waste water			
Acceptable	**100%**	100%	100%
OAEM	**0%**	0%	0%
Substandard/doubtful	**0%**	0%	0%
	100%	100%	100%
Rural residential real estate			
Acceptable	**97%**	95%	91%
OAEM	**1%**	1%	1%
Substandard/doubtful	**2%**	4%	8%
	100%	100%	100%
Total Loans			
Acceptable	**95%**	95%	94%
OAEM	**4%**	4%	3%
Substandard/doubtful	**1%**	1%	3%
	100%	100%	100%

The following tables provide an age analysis of past due loans (including accrued interest) as of December 31, 2018, 2017 and 2016:

December 31, 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	**$ 2,622,847**	**$ 732,799**	**$ 3,355,646**	**$ 1,257,465,669**	**$ 1,260,821,315**
Production and intermediate term	**10,470**	**47,546**	**58,016**	**93,970,764**	**94,028,780**
Loans to cooperatives	**-**	**-**	**-**	**8,739,066**	**8,739,066**
Processing and marketing	**-**	**-**	**-**	**130,279,773**	**130,279,773**
Farm-related business	**-**	**-**	**-**	**12,765,501**	**12,765,501**
Communication	**-**	**-**	**-**	**8,958,923**	**8,958,923**
Energy	**85,370**	**-**	**85,370**	**37,806,152**	**37,891,522**
Water and waste water	**-**	**-**	**-**	**4,952,834**	**4,952,834**
Rural residential real estate	**9,064**	**121,085**	**130,149**	**10,035,039**	**10,165,188**
Total	**$ 2,727,751**	**$ 901,430**	**$ 3,629,181**	**$ 1,564,973,721**	**$ 1,568,602,902**

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	$ 1,354,146,637	$ 1,357,624,407
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	13,416,431	13,717,883
Total	$ 2,971,839	$ 2,241,072	$ 5,212,911	$ 1,685,181,013	$ 1,690,393,924

December 31, 2016:	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or less than 30 Days Past Due	Total Loans
Real estate mortgage	$ 964,121	$ 517,454	$ 1,481,575	$ 1,305,400,443	$ 1,306,882,018
Production and intermediate term	1,177,454	110,821	1,288,275	127,851,130	129,139,405
Loans to cooperatives	-	-	-	14,576,489	14,576,489
Processing and marketing	-	-	-	118,138,963	118,138,963
Farm-related business	-	-	-	13,549,986	13,549,986
Communication	-	-	-	8,069,218	8,069,218
Energy	-	-	-	45,468,243	45,468,243
Water and waste water	-	-	-	6,406,716	6,406,716
Rural residential real estate	43,803	701,898	745,701	14,359,311	15,105,012
Total	$ 2,185,378	$ 1,330,173	$ 3,515,551	$ 1,653,820,499	$ 1,657,336,050

Troubled Debt Restructuring: 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, 2018, the total recorded investment of troubled debt restructured loans was $2,009,732 including $535,232 classified as nonaccrual and $1,474,500 classified as accrual, with specific allowance for loan losses of $131,733. As of December 31, 2018, commitments to lend funds to borrowers whose loan terms have been modified in a troubled debt restructuring were $0.

The following tables present additional information regarding troubled debt restructurings, which includes both accrual and nonaccrual loans with troubled debt restructuring designation, that occurred during the years ended December 31, 2018, 2017 and 2016. The pre-modification outstanding recorded investment represents the recorded investment of the loans as of the quarter end prior to the restructuring. The post-modification outstanding recorded investment represents the recorded investment of the loans as of the quarter end the restructuring occurred.

December 31, 2018:	**Pre-modification Outstanding Recorded Investment**	**Post-modification 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**

December 31, 2017:	Pre-modification Outstanding Recorded Investment	Post-modification Outstanding Recorded Investment
Troubled debt restructurings:		
Production and intermediate term	$ 2,212,160	$ 1,708,217
Total	$ 2,212,160	$ 1,708,217

December 31, 2016:	Pre-modification Outstanding Recorded Investment	Post-modification Outstanding Recorded Investment
Troubled debt restructurings:		
Real estate mortgage	$ 86,863	$ 85,388
Total	$ 86,863	$ 85,388

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). Charge-offs recorded at the modification date were $0 for the year ending December 31, 2018.

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.

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, 2018**	Recorded Investment at December 31, 2017	Recorded Investment at December 31, 2016
Real estate mortgage	**$ -**	$ -	$ 88,140
Total	**$ -**	$ -	$ 88,140

There were no additional commitments to lend to borrowers whose loans have been modified in TDRs at December 31, 2018, 2017 or 2016.

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, 2018	December 31, 2017	December 31, 2016
Troubled debt restructurings:			
Real estate mortgage	**$ 497,525**	$ 3,297,717	$ 3,358,316
Production and intermediate term	**1,391,122**	1,708,217	-
Rural residential real estate	**121,085**	-	-
Total	**$ 2,009,732**	$ 5,005,934	$ 3,358,316

	TDRs on Nonaccrual Status*		
	December 31, 2018	December 31, 2017	December 31, 2016
Troubled debt restructurings:			
Real estate mortgage	**$ 388,407**	$ 218,806	$ 252,284
Production and intermediate term	**25,740**	249,790	-
Rural residential real estate	**121,085**	-	-
Total	**$ 535,232**	$ 468,596	$ 252,284

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

Additional impaired loan information

	Recorded Investment at 12/31/2018	Unpaid Principal Balance[a]	Related Allowance	Average Impaired Loans	Interest Income Recognized
Impaired loans with a related allowance for credit losses:					
Real estate mortgage	$ 569,621	$ 649,861	$ 136,829	$ 535,521	$ 3,455
Production and intermediate term	21,363	85,499	4,450	315,883	2,325
Rural residential real estate	121,085	168,942	49,207	75,258	2,243
Total	$ 712,069	$ 904,302	$ 190,486	$ 926,662	$ 8,023
Impaired loans with no related allowance for credit losses:					
Real estate mortgage	$ 3,695,688	$ 3,779,159	$ -	$ 4,383,711	$ 58,083
Production and intermediate term	1,391,565	2,469,221	-	1,591,658	113,771
Rural residential real estate	31,208	31,404	-	42,371	-
Total	$ 5,118,461	$ 6,279,784	$ -	$ 6,017,740	$ 171,854
Total impaired loans:					
Real estate mortgage	$ 4,265,309	$ 4,429,020	$ 136,829	$ 4,919,232	$ 61,538
Production and intermediate term	1,412,928	2,554,720	4,450	1,907,541	116,096
Rural residential real estate	152,293	200,346	49,207	117,629	2,243
Total	$ 5,830,530	$ 7,184,086	$ 190,486	$ 6,944,402	$ 179,877

	Recorded Investment at 12/31/2017	Unpaid Principal Balance[a]	Related Allowance	Average Impaired Loans	Interest Income Recognized
Impaired loans with a related allowance for credit losses:					
Real estate mortgage	$ 160,483	$ 214,343	$ 46,363	$ 453,368	$ 6,764
Production and intermediate term	797,585	1,465,175	302,611	1,052,600	4,431
Farm-related business	-	-	-	-	-
Rural residential real estate	-	-	-	182,890	-
Total	$ 958,068	$ 1,679,518	$ 348,974	$ 1,688,858	$ 11,195
Impaired loans with no related allowance for credit losses:					
Real estate mortgage	$ 6,811,711	$ 6,810,197	$ -	$ 7,249,520	$ 1,131,234
Production and intermediate term	2,172,484	2,797,932	-	976,216	26,502
Farm-related business	-	-	-	-	18,851
Rural residential real estate	228,181	228,377	-	534,306	35,798
Total	$ 9,212,376	$ 9,836,506	$ -	$ 8,760,042	$ 1,212,385
Total impaired loans:					
Real estate mortgage	$ 6,972,194	$ 7,024,540	$ 46,363	$ 7,702,888	$ 1,137,998
Production and intermediate term	2,970,069	4,263,107	302,611	2,028,816	30,933
Farm-related business	-	-	-	-	18,851
Rural residential real estate	228,181	228,377	-	717,196	35,798
Total	$ 10,170,444	$ 11,516,024	$ 348,974	$ 10,448,900	$ 1,223,580

	Recorded Investment at 12/31/2016	Unpaid Principal Balance[a]	Related Allowance	Average Impaired Loans	Interest Income Recognized
Impaired loans with a related allowance for credit losses:					
Real estate mortgage	$ 559,032	$ 559,032	$ 21,683	$ 325,567	$ 1,946
Production and intermediate term	997,749	997,749	327,955	73,298	18,370
Farm-related business	-	-	-	-	-
Rural residential real estate	-	-	-	109,025	-
Total	$ 1,556,781	$ 1,556,781	$ 349,638	$ 507,890	$ 20,316
Impaired loans with no related allowance for credit losses:					
Real estate mortgage	$ 5,749,364	$ 5,746,870	$ -	$ 5,983,951	$ 306,029
Production and intermediate term	1,119,567	1,450,405	-	228,306	61,573
Farm-related business	-	-	-	-	9,574
Rural residential real estate	887,983	888,177	-	537,837	2,559
Total	$ 7,756,914	$ 8,085,452	$ -	$ 6,750,094	$ 379,735
Total impaired loans:					
Real estate mortgage	$ 6,308,396	$ 6,305,902	$ 21,683	$ 6,309,518	$ 307,975
Production and intermediate term	2,117,316	2,448,154	327,955	301,604	79,943
Farm-related business	-	-	-	-	9,574
Rural residential real estate	887,983	888,177	-	646,862	2,559
Total	$ 9,313,695	$ 9,642,233	$ 349,638	$ 7,257,984	$ 400,051

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

There were no material commitments to lend additional funds to debtors whose loans were classified as impaired at December 31, 2018, 2017 and 2016.

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

	2018	2017	2016
Interest income which would have been recognized under the original terms	**$ 621,243**	$ 1,701,063	$ 1,099,102
Less: interest income recognized	**(179,877)**	(1,223,580)	(400,051)
Foregone interest income	**$ 441,366**	$ 477,483	$ 699,051

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

	Real Estate Mortgage	Production & Intermediate Term	Agribusiness	Communication	Energy	Water & Waste Water	Rural Residential Real Estate	Total
Allowance for Credit Losses:								
Balance at December 31, 2017	$ 6,775,679	$ 1,510,355	$ 530,851	$ 15,578	$ 38,826	$ 149,622	$ 161,086	$ 9,181,997
Charge-offs	(108,113)	(637,236)	-	-	-	-	(47,857)	(793,206)
Recoveries	27,873	360,471	302,810	-	-	-	-	691,154
Provision for loan losses	(201,490)	121,654	(505,595)	(2,891)	(14,530)	37,751	(10,618)	(575,719)
Other	3,629	102,556	22,384	96	(532)	13,071	-	141,204
Balance at December 31, 2018	$ 6,497,578	$ 1,457,800	$ 350,450	$ 12,783	$ 23,764	$ 200,444	$ 102,611	$ 8,645,430
Ending Balance: individually evaluated for impairment	$ 136,829	$ 4,450	$ -	$ -	$ -	$ -	$ 49,207	$ 190,486
Ending Balance: collectively evaluated for impairment	$ 6,360,749	$ 1,453,350	$ 350,450	$ 12,783	$ 23,764	$ 200,444	$ 53,404	$ 8,454,944
Recorded Investment in Loans Outstanding:								
Ending Balance at December 31, 2018	$1,260,821,315	$ 94,028,780	$ 151,784,340	$ 8,958,923	$ 37,891,522	$ 4,952,834	$ 10,165,188	$1,568,602,902
Ending balance for loans individually evaluated for impairment	$ 4,265,309	$ 1,412,928	$ -	$ -	$ -	$ -	$ 152,293	$ 5,830,530
Ending balance for loans collectively evaluated for impairment	$1,256,556,006	$ 92,615,852	$ 151,784,340	$ 8,958,923	$ 37,891,522	$ 4,952,834	$ 10,012,895	$1,562,772,372

	Real Estate Mortgage	Production and Intermediate Term	Agribusiness	Communication	Energy	Water and Waste Water	Rural Residential Real Estate	Total
Allowance for Credit Losses:								
Balance at December 31, 2016	$ 7,306,321	$ 1,966,085	$ 584,077	$ 14,320	$ 66,634	$ 71,447	$ 62,863	$ 10,071,747
Charge-offs	(115,533)	(724,521)	-	-	-	-	-	(840,054)
Recoveries	19,232	124,887	548,676	-	-	-	-	692,795
Provision for loan losses	(436,986)	279,316	(609,933)	470	(27,180)	65,947	98,223	(630,143)
Other	2,645	(135,412)	8,031	788	(628)	12,228	-	(112,348)
Balance at December 31, 2017	$ 6,775,679	$ 1,510,355	$ 530,851	$ 15,578	$ 38,826	$ 149,622	$ 161,086	$ 9,181,997
Ending Balance: individually evaluated for impairment	$ 46,363	$ 302,611	$ -	$ -	$ -	$ -	$ -	$ 348,974
Ending Balance: collectively evaluated for impairment	$ 6,729,316	$ 1,207,744	$ 530,851	$ 15,578	$ 38,826	$ 149,622	$ 161,086	$ 8,833,023
Recorded Investment in Loans Outstanding:								
Ending Balance at December 31, 2017	$1,357,624,407	$107,402,571	$ 157,398,491	$ 8,731,512	$ 42,156,596	$ 3,362,464	$ 13,717,883	$1,690,393,924
Ending balance for loans individually evaluated for impairment	$ 6,950,507	$ 2,970,069	$ -	$ -	$ -	$ -	$ 228,182	$ 10,148,758
Ending balance for loans collectively evaluated for impairment	$1,350,652,214	$104,432,502	$ 157,398,491	$ 8,731,512	$ 42,156,596	$ 3,362,464	$ 13,489,701	$1,680,223,480
Ending balance for loans acquired with deteriorated credit quality	$ 21,686	$ -	$ -	$ -	$ -	$ -	$ -	$ 21,686

	Real Estate Mortgage	Production and Intermediate Term	Agribusiness	Communication	Energy	Water and Waste Water	Rural Residential Real Estate	Total
Allowance for Credit Losses:								
Balance at December 31, 2015	$ 5,884,916	$ 299,660	$ 285,442	$ 88,173	$ 94,434	$ 6,262	$ 158,534	$ 6,817,421
Charge-offs	(34,534)	-	-	-	-	-	-	(34,534)
Recoveries	2,769	82,919	429,679	-	-	-	-	515,367
Provision for loan losses	1,452,132	1,600,584	(111,630)	(75,315)	(41,802)	92,755	(96,067)	2,820,657
Other	1,038	(17,078)	(19,414)	1,462	14,002	(27,570)	396	(47,164)
Balance at December 31, 2016	$ 7,306,321	$ 1,966,085	$ 584,077	$ 14,320	$ 66,634	$ 71,447	$ 62,863	$ 10,071,747
Ending Balance: individually evaluated for impairment	$ 21,683	$ 327,955	$ -	$ -	$ -	$ -	$ -	$ 349,638
Ending Balance: collectively evaluated for impairment	$ 7,284,638	$ 1,638,130	$ 584,077	$ 14,320	$ 66,634	$ 71,447	$ 62,863	$ 9,722,109
Recorded Investment in Loans Outstanding:								
Ending Balance at December 31, 2016	$1,306,882,018	$129,139,405	$ 146,265,438	$ 8,069,218	$ 45,468,243	$ 6,406,716	$ 15,105,012	$1,657,336,050
Ending balance for loans individually evaluated for impairment	$ 6,087,438	$ 2,107,540	$ -	$ -	$ -	$ -	$ 887,983	$ 9,082,961
Ending balance for loans collectively evaluated for impairment	$1,300,573,622	$127,022,089	$ 146,265,438	$ 8,069,218	$ 45,468,243	$ 6,406,716	$ 14,217,029	$1,648,022,355
Ending balance for loans acquired with deteriorated credit quality	$ 220,958	$ 9,776	$ -	$ -	$ -	$ -	$ -	$ 230,734

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

The Association operates under a General Financing Agreement (GFA) with the Bank. The current GFA is effective through September 30, 2020. The investment in the Farm Credit Bank of Texas is a requirement of borrowing from the Bank and is carried at cost plus allocated equities, not fair value, in the accompanying balance sheet. Estimating the fair value of the Association's investment in the Farm Credit Bank of Texas is not practicable because the stock is not traded. The Association owns 8.39% of the issued stock of the Bank as of December 31, 2018. As of that date, the Bank's assets totaled $24.5 billion and members' equity totaled $1.8 billion. The Bank's earnings were $191 million during 2018.

NOTE 6 — PREMISES AND EQUIPMENT:

Premises and equipment consisted of the following at December 31:

	2018	2017	2016
Land and improvements	**$ 564,498**	$ 564,498	$ 564,498
Building and improvements	**2,998,396**	3,017,034	2,988,283
Furniture and equipment	**388,969**	413,835	422,231
Computer equipment and software	**895,052**	853,568	741,465
Automobiles	**1,779,855**	1,489,962	1,216,796
Construction in progress	**5,673**	-	-
	6,632,443	6,338,897	5,933,273
Accumulated depreciation	**(3,543,807)**	(3,503,317)	(2,772,915)
Total	**$ 3,088,636**	$ 2,835,580	$ 3,160,358

The Association leases office space in Fort Worth, Sherman, Abilene, Weatherford and Georgetown. Lease expense was $553,001, $505,998 and $521,035 for 2018, 2017 and 2016, respectively. None of the Association's leases qualify for capital lease treatment and all are considered operating leases. Minimum annual lease payments for the next five years are as follows:

	Operating
2019	$ 547,299
2020	555,522
2021	391,601
2022	53,833
2023	-
Thereafter	-
Total	$ 1,548,255

NOTE 7 — OTHER PROPERTY OWNED, NET:

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

	2018	2017	2016
Gain (loss) on sale, net	**$ 26,318**	$ 93,452	$ 77,026
Operating income (expense), net	**(2,595)**	(504)	(846)
Net gain (loss) on other property owned	**$ 23,723**	$ 92,948	$ 76,180

NOTE 8 — OTHER ASSETS AND OTHER LIABILITIES:

Other assets comprised the following at December 31:

	2018	2017	2016
Accounts receivable (other than members)	**$ 804,467**	$ 772,517	$ 737,373
Other assets	**556,058**	188,954	151,775
Total	**$ 1,360,525**	$ 961,471	$ 889,148

Other liabilities comprised the following at December 31:

	2018	2017	2016
Accounts payable	**$ 4,807,598**	$ 5,349,996	$ 6,763,089
Accumulated postretirement obligation	**4,691,921**	5,453,355	4,754,167
Funds held/advanced conditional payments	**29,317**	26,185	64,684
Other liabilities	**1,097,785**	894,368	1,016,382
Total	**$ 10,626,621**	$ 11,723,904	$ 12,598,322

NOTE 9 — 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 GFA. 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 GFA, which is September 30, 2020, unless terminated sooner 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, 2018, 2017 and 2016, was $1,216,709,990 at 2.72 percent, $1,358,683,640 at 2.29 percent and $1,320,377,658 at 2.05 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, 2018, 2017 and 2016, the Association’s note payable was within the specified limitations. The maximum amount the Association may borrow from the Bank as of December 31, 2018 was $1,495,465,641, as defined by the GFA.

In addition to borrowing limits, the GFA 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 GFA associated with the covenants include additional reporting requirements, development of action plans, reduction of lending limits or repayment of indebtedness, and increases in interest rates on indebtedness. 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 met the waiver conditions and is no longer in default of the GFA.

NOTE 10 — MEMBERS’ EQUITY:

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

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

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

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

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

Within two years of repayment of a loan, the Association capital bylaws require the conversion of any borrower's outstanding Class B 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 Class A shares is made solely at the discretion of the Association's Board of Directors. At December 31, 2018, 2017 and 2016, the Association had 1,989, 600 and 0, respectively, of Class A stock issued and outstanding.

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

Dividends and patronage distributions may be paid on the capital stock and participation certificates of the Association, as the Board of Directors may determine by resolution, subject to capitalization requirements as defined by the FCA. Amounts not distributed are retained as unallocated retained earnings. The following dividends and patronage distributions were declared and paid as follows:

Date Declared	Date Paid (to be Paid)	Patronage
December 2018	March 2019	$ 20,377,032
July 2018	September 2018	7,049,954
December 2016	March 2017	13,824,603
October 2016	November 2017	3,000,029
December 2015	March 2016	12,923,433
October 2015	November 2015	4,115,377

As a result of the merger in 2014, the Association recognized $91,343,553 in additional paid-in capital (APIC). The APIC represents the excess value received over the par value of capital stock and participation certificates issued and arose from the issuance of the Association's capital stock and participation certificates in connection with the acquisition of Texas Land Bank, ACA.

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-adjusted assets are calculated differently than in the past. As of December 31, 2018, the Association is not prohibited from retiring stock or distributing earnings.

The following sets forth the regulatory capital ratio requirements and ratios at December 31, 2018:

Risk-adjusted:	**Regulatory Minimums**	**Conservation Buffer***	**Total**	**As of December 31, 2018**
Common equity tier 1 ratio	4.50%	2.50%	7.00%	19.87%
Tier 1 capital ratio	6.00%	2.50%	8.50%	19.87%
Total capital ratio	8.00%	2.50%	10.50%	20.44%
Permanent capital ratio	7.00%	0.00%	7.00%	19.98%
Non-risk-adjusted:				
Tier 1 leverage ratio**	4.00%	1.00%	5.00%	20.68%
UREE leverage ratio	1.50%	0.00%	1.50%	22.04%

*The 2.5% capital conservation buffer for the risk-adjusted ratios will be phased in over a three-year period ending on December 31, 2019. There is no phase-in of the leverage buffer.

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

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 are calculated differently for the permanent capital ratio (referred to 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 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, and 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.

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

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

	2018	2017	2016
Class A stock	**1,989**	600	-
Class B stock	**1,138,689**	1,223,949	1,230,121
Participation certificates	**41,550**	52,824	56,240
Total	**1,182,228**	1,277,373	1,286,361

An additional component of equity is accumulated other comprehensive loss (AOCL), which is reported net of taxes. As of December 31, 2018, 2017 and 2016, the balance of AOCL represented net actuarial gains and prior service credits related to other postretirement benefits of $399,101, $1,357,769 and $833,008, respectively.

NOTE 11 — INCOME TAXES:

The enactment of federal tax legislation in late December 2017, among other things, lowered the federal corporate tax rate from 35 percent to 21 percent beginning in 2018. In accordance with GAAP, the change to the lower corporate tax rate led to a revaluation of our deferred tax liabilities and deferred tax assets in the period of enactment (2017). The provision for income taxes in 2017 was mainly due to a decrease in deferred tax assets with a corresponding valuation allowance resulting from the enactment of federal tax legislation in late December 2017 which, among other things, lowered the federal corporate tax rate from 35 percent to 21 percent beginning in 2018. As the Association has a full valuation allowance recorded against its deferred tax assets, there is no impact to income tax expense as a result of the revaluation. The calculation of tax assets involves various management estimates and assumptions as to the future taxable earnings, including the following at December 31, 2018. The expected future tax rates are based upon enacted tax laws.

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

	2018	2017	2016
Current:			
State	**$ -**	$ -	$ -
Total current	**-**	-	-
Deferred:			
Federal	**23,608**	1,144	(24)
Total deferred	**23,608**	1,144	(24)
Total provision for (benefit from) income taxes	**$ 23,608**	$ 1,144	$ (24)

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:

	2018	2017	2016
Federal tax at statutory rate	**$ 6,163,979**	$ 4,056,180	$ 6,550,677
Effect of nontaxable FLCA subsidiary	**$ (6,679,102)**	(4,382,263)	(8,381,555)
Change in valuation allowance	**538,731**	(5,799,941)	1,774,463
Change in effective tax rate	**-**	6,127,168	52,310
Other	**-**	-	4,081
Provision for (benefit from) income taxes	**$ 23,608**	$ 1,144	$ (24)

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

	2018	2017	2016
Deferred Tax Assets			
Allowance for loan losses	**$ 115,946**	$ 340,941	$ 593,727
Loss carryforwards	**10,396,166**	9,632,440	15,179,595
Gross deferred tax assets	**10,512,112**	9,973,381	15,773,322
Deferred tax asset valuation allowance	**(10,512,112)**	(9,973,381)	(15,773,322)
Deferred Tax Liabilities			
Other	**(114,308)**	(90,700)	(89,556)
Gross deferred tax liabilities	**(114,308)**	(90,700)	(89,556)
Net deferred tax asset (liability)	**$ (114,308)**	$ (90,700)	$ (89,556)

The Association recorded valuation allowances of $10,512,112, $9,973,381 and $15,773,322 during 2018, 2017 and 2016, respectively. The Association will continue to evaluate the realizability of the deferred tax assets and adjust the valuation allowance accordingly.

NOTE 12 — EMPLOYEE BENEFIT PLANS:

Employee Retirement Plans: Employees of the Association participate in either the defined benefit retirement plan (DB plan) or the defined contributions plan (DC plan) and are eligible to participate in the Farm Credit Benefits Alliance 401(k) Plan. 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 multi-employer, 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 executive 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 of 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 Restored Employer Contributions of $10,400, $17,731 and $32,943 made to this plan for the years ended December 31, 2018, 2017 and 2016. There were no payments made from the supplemental 401(k) plan to active employees during 2018, 2017 and 2016.

The DB plan is noncontributory and benefits are based on salary and years of service. The legal name of the plan is Farm Credit Bank of Texas Pension Plan; its employer identification number is 74-1110170. The DB plan is not subject to any contractual expiration dates. The DB plan's funding policy is to fund current year benefits expected to be earned by covered employees plus an amount to improve the accumulated benefit obligation funded status by a percentage approved by the plan sponsor. The plan sponsor is the board of the Farm Credit Bank of Texas. The "projected unit credit" actuarial method is used for both financial reporting and funding purposes. District employers have the option of providing enhanced retirement benefits, under certain conditions, within the DB plan, to facilitate reorganization and/or restructuring. The actuarial present value of vested and nonvested accumulated benefit obligation exceeded the net assets of the DB plan as of December 31, 2018.

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

a. Assets contributed to the multi-employer 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 multi-employer 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, 2018, 2017 and 2016:

	2018	2017	2016
Funded status of plan	**68.0** %	69.7 %	66.4 %
Association's contribution	**$ 744,934**	$ 1,156,528	$ 625,890
Percentage of association's contribution to total contributions	**7.6** %	10.0 %	5.3 %

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 70.1 percent, 73.4 percent and 70.6 percent at December 31, 2018, 2017 and 2016, respectively.

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

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

Retiree Welfare Benefit Plans

Disclosure Information Related to Retirement Benefits	**2018**	2017	2016
Change in Accumulated Postretirement Benefit Obligation			
Accumulated postretirement benefit obligation, beginning of year	**$ 5,453,356**	$ 4,754,167	$ 4,573,751
Service cost	**100,209**	89,659	77,737
Interest cost	**215,203**	215,401	211,483
Plan participants' contributions	**88,856**	67,139	45,003
Plan amendments	**(221,128)**	-	-
Special termination benefits	**-**	-	-
Actuarial loss (gain)	**(678,300)**	532,975	26,203
Benefits paid	**(266,275)**	(205,985)	(180,010)
Accumulated postretirement benefit obligation, end of year	**$ 4,691,921**	$ 5,453,356	$ 4,754,167
Change in Plan Assets			
Plan assets at fair value, beginning of year	**$ -**	$ -	$ -
Actual return on plan assets	**-**	-	-
Company contributions	**177,419**	138,846	135,007
Plan participants' contributions	**88,856**	67,139	45,003
Benefits paid	**(266,275)**	(205,985)	(180,010)
Plan assets at fair value, end of year	**$ -**	$ -	$ -
Funded status of the plan	**$ (4,691,921)**	$ (5,453,356)	$ (4,754,167)
Amounts Recognized in Statement of Financial Position			
Other liabilities	**$ (4,691,921)**	$ (5,453,356)	$ (4,754,167)
Amounts Recognized in Accumulated Other Comprehensive Income			
Net actuarial loss (gain)	**$ 620,229**	$ 1,383,838	$ 893,834
Prior service cost (credit)	**(221,128)**	(26,069)	(60,826)
Net transition obligation (asset)	**-**	-	-
Total	**$ 399,101**	$ 1,357,769	$ 833,008
Weighted-Average Assumptions Used to Determine Obligations at Year End			
Measurement date	**12/31/2018**	12/31/2017	12/31/2016
Discount rate	**4.75%**	4.00%	4.60%
Health care cost trend rate assumed for next year (pre-/post-65) - medical	**7.30%/6.90%**	7.70%/6.90%	6.75%/6.50%
Health care cost trend rate assumed for next year - Rx	**6.90%**	6.90%	6.50%
Ultimate health care cost trend rate	**4.50%**	4.50%	4.50%
Year that the rate reaches the ultimate trend rate	**2027**	2026	2025

Total Cost	**2018**	2017	2016
Service cost	**$ 100,209**	$ 89,659	$ 77,737
Interest cost	**215,203**	215,401	211,483
Expected return on plan assets	**-**	-	-
Amortization of:			
Unrecognized net transition obligation (asset)	**-**	-	-
Unrecognized prior service cost	**(26,069)**	(34,757)	(34,757)
Unrecognized net loss (gain)	**85,309**	42,971	48,702
Net postretirement benefit cost	**$ 374,652**	$ 313,274	$ 303,165
Accounting for settlements/curtailments/special termination benefits	**$ -**	$ -	$ -
Other Changes in Plan Assets and Projected Benefit Obligation Recognized in Other Comprehensive Income			
Net actuarial loss (gain)	**$ (678,300)**	$ 532,975	$ 26,203
Amortization of net actuarial loss (gain)	**(85,309)**	(42,971)	(48,702)
Prior service cost (credit)	**(221,128)**	-	-
Amortization of prior service cost	**26,069**	34,757	34,757
Recognition of prior service cost		-	-
Amortization of transition liability (asset)	**-**	-	-
Total recognized in other comprehensive income	**$ (958,668)**	$ 524,761	$ 12,258
AOCI Amounts Expected to be Amortized Into Expense in 2019			
Unrecognized net transition obligation (asset)	**$ -**	$ -	$ -
Unrecognized prior service cost	**(26,514)**	(26,069)	(34,757)
Unrecognized net loss (gain)	**15,932**	85,309	42,971
Total	**$ (10,582)**	$ 59,240	$ 8,214
Weighted-Average Assumptions Used to Determine Benefit Cost			
Measurement date	**12/31/2018**	12/31/2016	12/31/2015
Discount rate	**4.00%**	4.60%	4.70%
Health care cost trend rate assumed for next year (pre-/post-65) - medical	**7.70%/6.90%**	6.75%/6.50%	7.00%/6.50%
Health care cost trend rate assumed for next year - Rx	**4.50%**	6.50%	6.50%
Ultimate health care cost trend rate	**4.50%**	4.50%	4.50%
Year that the rate reaches the ultimate trend rate	**2026**	2025	2025

Expected Future Cash Flows

Expected Benefit Payments (net of employee contributions)			
Fiscal 2019	**$ 198,179**	$ 192,610	$ 197,922
Fiscal 2020	**207,291**	205,109	207,895
Fiscal 2021	**212,420**	210,425	212,833
Fiscal 2022	**211,669**	212,159	1,121,030
Fiscal 2023	**229,666**	1,188,027	-
Fiscal 2024-2028	**1,171,606**	-	-
Expected Contributions			
Fiscal 2019	**$ 198,179**	$ 192,610	$ 197,922

NOTE 13 — 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 employees, 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 $21,349,726, $21,191,584 and $24,321,661 at December 31, 2018, 2017 and 2016, respectively. During 2018, $27,177,190 of new loans were made, and repayments totaled $27,019,048. In the opinion of management, no such loans outstanding at December 31, 2018, 2017 and 2016 involved more than a normal risk of collectability.

Expenses included in purchased services 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 $99,333, $116,712 and $115,502 in 2018, 2017 and 2016, respectively.

The Association received patronage payments from the Bank totaling $6,591,895, $6,237,662 and $6,151,906 during 2018, 2017 and 2016, respectively.

NOTE 14 — 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.

	Valuation Technique(s)	Input
Cash	Carrying value	Par/principal and appropriate interest yield
Loans	Discounted cash flow	Prepayment forecasts Probability of default Loss severity
Fair value of concessions granted	Discounted cash flow	Loan terms Market interest rates
Other interest bearing liabilities	Carrying value	Par/principal and appropriate interest yield

Assets and liabilities measured at fair value on a recurring basis at December 31, 2018, 2017 and 2016 only include nonqualified benefit trusts. This level 1 asset was $159,320, $164,094, and $134,688 at December 31, 2018, 2017 and 2016, respectively.

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

December 31, 2018	**Fair Value Measurement Using**			**Total Fair**
	Level 1	**Level 2**	**Level 3**	**Value**
Assets:				
Loans	**$ -**	**$ -**	**$ 515,785**	**$ 515,785**

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

December 31, 2016	Fair Value Measurement Using			Total Fair
	Level 1	Level 2	Level 3	Value
Assets:				
Loans	$ -	$ -	$1,168,534	$1,168,534

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, 2018
Fair Value Measurement Using

	Total Carrying Amount	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**
Assets:					
Cash	**$ 100,291**	**$ 100,291**	**$ -**	**$ -**	**$ 100,291**
Net loans	**1,550,457,948**	**-**	**-**	**1,497,146,168**	**1,497,146,168**
Total Assets	**$ 1,550,558,239**	**$ 100,291**	**$ -**	**$ 1,497,146,168**	**$ 1,497,246,459**
Liabilities:					
Note payable to bank	**$ 1,216,709,990**	**$ -**	**$ -**	**$ 1,175,102,109**	**$ 1,175,102,109**

December 31, 2017
Fair Value Measurement Using

	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
Assets:					
Cash	$ 90,437	$ 90,437	$ -	$ -	$ 90,437
Net loans	1,671,281,511	-	-	1,633,382,529	1,633,382,529
Total Assets	$ 1,671,371,948	$ 90,437	$ -	$ 1,633,382,529	$ 1,633,472,966
Liabilities:					
Note payable to bank	$ 1,358,683,640	$ -	$ -	$ 1,316,386,750	$ 1,316,386,750

December 31, 2016
Fair Value Measurement Using

	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
Assets:					
Cash	$ 60,478	$ 60,478	$ -	$ -	$ 60,478
Net loans	1,636,926,241	-	-	1,609,245,941	1,609,245,941
Total Assets	$ 1,636,986,719	$ 60,478	$ -	$ 1,609,245,941	$ 1,609,306,419
Liabilities:					
Note payable to bank	$ 1,320,377,658	$ -	$ -	$ 1,295,730,638	$ 1,295,730,638

Valuation Techniques

As more fully discussed in Note 3, “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:

Investments

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.

Fair Value of Concessions Granted

The Association has recorded amounts related to the fair value of concessions granted for certain loans related to the breach of Association policies in 2016 and 2017. These amounts are netted against the unpaid principal balance of the related loans similar to a discount. The concessions granted were either through the refinancing of a relationship or as a result of acceptance of rates and terms previously negotiated, which were more favorable than market terms and rates. The fair value of the concessions are based on the expected future cash flows under the new contractual terms, discounted at a market interest rate. The fair value of the concessions is amortized into interest income over the contractual life of the related loans. The unpaid principal balance of loans with discounts for the fair value of concessions granted were $69,688,230, $72,205,060 and $9,605,594 as of December 31, 2018, 2017 and 2016, respectively. The unaccreted fair value of concessions at December 31, 2018, 2017 and 2016 was $13,760,082, $14,624,894 and $2,141,609, respectively. Amounts accreted into interest income for the years ended December 31, 2018, 2017 and 2016 was $864,813, $181,820 and $13,279, respectively.

Other Property Owned

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

NOTE 15 — COMMITMENTS AND CONTINGENCIES:

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

The Association may participate in financial instruments with off-balance-sheet risk to satisfy the financing needs of its borrowers in the form of commitments to extend credit and commercial letters of credit. These financial instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the financial statements. Commitments to extend credit are agreements to lend to a borrower as long as there is not a violation of any condition established in the contract. Commercial letters of credit are agreements to pay a beneficiary under conditions specified in the letter of credit. Commitments and letters of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee. At December 31, 2018, the Association had outstanding commitments of $172,857,162 to extend credit.

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

NOTE 16 — QUARTERLY FINANCIAL INFORMATION (UNAUDITED):

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

	2018				
	First	**Second**	**Third**	**Fourth**	**Total**
Net interest income	**$ 11,867**	**$ 14,190**	**$ 11,061**	**$ 10,907**	**$ 48,025**
(Provision for) reversal of loan losses	**1,193**	**(38)**	**(1,053)**	**474**	**576**
Noninterest income (expense), net	**(3,486)**	**(4,990)**	**(5,571)**	**(4,924)**	**(18,971)**
Net income	**$ 9,574**	**$ 9,162**	**$ 4,437**	**$ 6,457**	**$ 29,630**

	2017				
	First	Second	Third	Fourth	Total
Net interest income	$ 11,707	$ 11,576	$ 11,992	$ 11,769	$ 47,044
(Provision for) reversal of loan losses	54	(725)	(2,075)	3,376	630
Noninterest income (expense), net	(11,434)	(5,453)	(11,348)	(7,851)	(36,086)
Net income	$ 327	$ 5,398	$ (1,431)	$ 7,294	$ 11,588

	2016				
	First	Second	Third	Fourth	Total
Net interest income	$ 10,762	$ 10,900	$ 11,200	$ 11,469	$ 44,331
(Provision for) reversal of loan losses	202	(225)	404	(3,202)	(2,821)
Noninterest income (expense), net	(3,682)	(4,102)	(4,460)	(10,550)	(22,794)
Net income	$ 7,282	$ 6,573	$ 7,144	$ (2,283)	$ 18,716

NOTE 17 — SUBSEQUENT EVENTS:

The Association has evaluated subsequent events through March 13, 2019, which is the date the consolidated financial statements were issued or available to be issued.

There are no subsequent events requiring disclosure as of March 13, 2019.

BOARD OF DIRECTORS

CORPORATE GOVERNANCE

At year end, the Board of Directors of Lone Star, ACA was comprised of 13 positions; two of which were vacant. Ten director positions are elected by the voting membership. Each represents one of eight geographic regions that comprise Lone Star, ACA's lending territory. One of the 10 member-elected directors resigned in October 2018 and another elected director was elected to the District Board in 2017. Three directors are appointed by the other members of the Board and cannot be customers, stockholders, employees or agents of any Farm Credit institution. Two of these appointed outside directors bring specific financial, accounting and audit expertise to the Board and one chairs the Board's Audit Committee and the Compliance Committee and the other serves as vice-chairman and also serves as Chairman of the Risk Committee. The other appointed outside director position is used to bring outside perspective and other areas of expertise to enhance board oversight capabilities.

In January 2019, the stockholders of Lone Star elected three new directors, Gil Flautt V, Cody Hughes, and Asa Langford, all of whom will serve a term of three years.

AUDIT COMMITTEE

As of December 31, 2018, this Committee was made up of five board members, including two appointed outside directors with financial expertise. All members of the Committee are expected to have practical knowledge of finance and accounting, be able to read and have a working understanding of the financial statements, or develop that understanding within a reasonable period of time after being appointed to the Committee. Don Crawford and David W. Conrad serve as chairman and vice-chairman, respectively, of the Committee. The Board of Directors has determined that Mr. Crawford and Mr. Conrad have the qualifications and experience necessary to serve as Audit Committee 'financial experts' as defined by FCA regulation, and have been designated as such. Other Audit Committee members as of December 31, 2018 were David Harris, Brent Neuhaus and Bert Pruett.

The Audit Committee members are appointed by the Board. All members of the Committee are independent of management for Lone Star, ACA or any system entity. The Audit Committee has unrestricted access to representatives of the internal audit firm, independent public accountants, internal credit review firms and financial management.

The Committee assists the Board in fulfilling its oversight responsibility related to accounting policies, internal controls, financial reporting practices and regulatory requirements. This Committee has a charter detailing its purpose and key objectives, authority, composition, meeting requirements and responsibilities. The charter, among other things, gives the Committee the authority to hire and compensate the internal and external auditors and credit reviewers, approve all audit and permitted non-audit services, review the audited financial statements and all public financial disclosures, meet privately with internal and external auditors and credit reviewers and review any complaints regarding accounting irregularities and fraud. The charter is posted on Lone Star, ACA's website at *www.lonestaragcredit.com*.

COMPENSATION COMMITTEE

The Compensation Committee consists of five Board members selected by the Board. Neither the CEO nor management can have any involvement in the selection of Committee members nor can they participate in any deliberations of the Committee on matters relating to their own compensation. The Committee is chaired by John Sawyer. Other Compensation Committee members as of December 31, 2018 were Harlin Brown, Richard Gaona, Chad Lee and Larry Stewart.

The Committee is responsible for reviewing and recommending for full Board approval the performance standards of the CEO and the evaluation of the CEO's performance against those standards. It also recommends to the Board all actions necessary to administer the CEO's compensation plan. The Board has delegated to the CEO the responsibility to administer the base salaries of senior officers and all other staff of Lone Star, ACA, within Board approved guidelines. However, the CEO must review the base salary administration with the Compensation Committee and the Committee recommends for Board approval the overall compensation program for senior officers. The Committee is also responsible for director compensation and for oversight of Lone Star, ACA's employee's salary and benefits plans and all Board policies applicable to those plans.

RISK COMMITTEE

The Risk Committee consists of three members appointed by the Board. Members of the Committee should have a working familiarity with general business and associated risks along with basic finance and accounting practices. The Committee is chaired by David Conrad and other members of the Risk Committee include David Harris and Chad Lee.

The Committee assists the Board in fulfilling its responsibilities related to the oversight of the Association's risk management policies and practices. Those policies and practices are applicable to strategic, credit, market, operational and reputation risk. The Committee helps position the Association to achieve and maintain a Financial Institution Rating System score of 2 or better, by continually evaluating the risk philosophy, appropriateness of the growth objectives, and risk management controls that appropriately balance risk and return. The Committee will establish credit and risk management policies consistent with the Association's risk philosophy and recommend changes from time to time as the risk profile of the Association changes.

DIRECTORS AND SENIOR OFFICERS

The Association's member-elected and director-elected Board of Directors and senior officers are as follows:

NAME	POSITION	DATE ELECTED/ EMPLOYED	TERM EXPIRES
David Harris	Chairman	2001	2019
John Sawyer	Vice Chairman	2014	2020
Steven Beakley	Director	2018	2019
Harlin Brown	Director	2013	2019
David Conrad	Director-Elected Outside Director	2014	2019
Don Crawford	Director-Elected Outside Director	2002	2019
Gil Flautt V	Director	2019	2021
Cody Hughes	Director	2019	2021
Asa Langford	Director	2019	2021
Chad Lee	Director-Elected Outside Director	2011	2019
Brent Neuhaus	Director	2016	2020
Bert Pruett	Director	1984	2020
Larry Stewart	Director	1984	2020
Bill Melton	Chief Executive Officer, Interim	2018	-
Amy Birt	Chief Financial Officer	2017	-
Jim Bob Reynolds	Chief Lending Officer	2010	-
Jeff Davis	Chief Operating Officer	2018	-
Sharmyn Calhoun-Alley	Chief Risk Officer	2018	-

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

David Harris was elected to the Board in 2001 and serves as the Association's Board Chairman and serves on the Risk and Compliance committees. Mr. Harris lives in Johnson County and owns property in Somervell, Johnson and Bosque counties. Mr. Harris is President of Bob Harris Oil Company, which is involved in retail gasoline marketing, ranching (cow-calf), real estate development and sand and gravel. He serves as the President of Harris Riverbend Farms, a purebred and commercial cow/calf operation, a partner in Mansfield Joint Venture, which is involved in warehouse development, the managing partner of Alvarado Joint Venture, which is involved in real estate development, a partner in Deli Partners, a deli and fast food operation, the managing partner in Brazos Aggregates, a sand and gravel operation and a director of Cleburne Economic Development Board. Mr. Harris serves on the Somervell County Livestock and Forage Performance Committee. He has previously served as President of the Premier Santa Gertrudis Association and Vice-President of Marketing for Santa Gertrudis Breeders International.

John R. Sawyer was elected to Texas Land Bank's Board in 2006, has served on the Association's Board since January 1, 2014 as a result of the merger, and is the Chairman of the Association's Compensation Committee and Vice Chairman of the Board. Mr. Sawyer resides in Hillsboro, Texas, is a farmer and rancher and operates Sawyer Farms Partnership, a farming operation that grows corn, milo, wheat and other specialty grains. Mr. Sawyer owns and operates Apex Grain Company, LLC, a grain elevator company located in Hillsboro, and he graduated from Texas A&M University with a BS in agronomy and a master of agriculture in ag economics. Mr. Sawyer is member of the Hillsboro Independent School District Board and First Baptist Church.

Steven Beakley is a resident in Ellis County, Texas and was appointed to the Board in 2018. Mr. Beakley farms and ranches in Ellis County where he raises cotton, corn, wheat and sunflowers, as well as maintains a cow-calf operation. He also operates Beakley Farms Grain in Bardwell, Texas and produces and sells certified seed as a WestBred Wheat Associate. Farming and ranching has been his principal occupation for the past 25 years. He graduated from Abilene Christian University with a BBA. Mr. Beakley is a member of his county Agrilife Extension Advisory Board, Vice President of Avalon Coop Gin, and is a representative for the Northern Blacklands zone of the Texas Boll Weevil Eradication Foundation, Inc. He previously served as the Chairman of the Grains Committee for Blackland Income Growth and was a member of the Ellis County Youth Expo Executive Committee.

Harlin Brown was elected to the Board in 2013. Mr. Brown lives in Woodland, Texas and is a full-time farmer and rancher. Mr. Brown has been in the logging and timber business for most of his life, runs a commercial cow-calf operation, manages timber on owned and leased property in Red River County, and grows hay in Choctaw County, Oklahoma. Mr. Brown serves as a Director of Red River Appraisal District and previously served on the Red River FSA County Committee and the 410 Water Supply Corporation. He has been a member of the Pine Creek Volunteer Fire Department for at least 25 years and has served in various capacities at the Woodland United Methodist Church.

David W. Conrad was elected to Texas Land Bank's Board in 2005 as a Director-Elected Director, has served on the Association's Board since January 1, 2014 as a result of the merger, and serves as the Chairman of the Risk Committee and Vice-Chairman of the Association's Audit Committee. Mr. Conrad resides in Round Rock, Texas, is a Certified Public Accountant, a partner in Pilot Peak Investments LLC, a commercial real estate rental company, and a member of the Texas Society of CPAs. Mr. Conrad was previously employed by the Farm Credit Bank of Texas from 1982 to 1990, where he served as Internal Auditor and Director of Association Financial Operations.

Don Crawford was elected to the Board in 2002 as a Director-Elected Director and serves as the Chairman of the Association's Audit Committee and Compliance Committee. Mr. Crawford resides in Palo Pinto County and is a Certified Public Accountant. He is a principal in Crawford, Carter and Durbin CPAs of Mineral Wells, a partner in Crawford Brothers Ranch of Strawn, Texas, a commercial beef cattle operation, and a general partner in Crawford Cross L, LP, a land holding company. Mr. Crawford is a Director and Chairman of the Audit Committee of Titan Bank, N.A. of Mineral Wells, Texas, a Director of Palo Pinto Municipal Water District #1, a Director and the Treasurer of Mineral Wells Industrial Foundation, a non-profit foundation, and Chairman of the Finance Committee of Our Lady of Lourdes Catholic Church in Mineral Wells, Texas.

Gil Flautt V is a resident of the Novice Community in the Blossom area of Lamar County, Texas and was elected to the Board in January 2019. Mr. Flautt is a self-employed rancher whose beef cattle operation includes cows, calves and yearlings. Ranching has been his principal occupation for the past five years. He earned a BS degree in agribusiness from Sam Houston State University and returned to his family's ranch upon graduation. He currently serves on the Paris Rodeo & Horse Club board. He is a member of the Texas Farm Bureau and the Novice Baptist Church. His wife is Celeste Flautt.

Cody Hughes was elected to the Board in 2019 and serves on the Audit Committee. Mr. Hughes was raised on a family farm in Roscoe, Texas and is a sixth generation farmer who farms cotton and wheat in Nolan, Mitchell and Fisher counties. Mr. Hughes farms individually and through a partnership with his father, CWH Farms. He and his wife Amy and two children reside on their farm south of Roscoe, where they also maintain a cow-calf operation. Before returning to farm full time, Mr. Hughes graduated from Tarleton State University with a degree in agricultural services and development. After college, he was employed by the United States Department of Agriculture, Farm Service Agency for seven years. He served as County Executive Director of Victoria, Gaines and Jones counties. Mr. Hughes currently serves as a member of the National Cotton Council, Nolan County Farm Bureau, Plains Cotton Cooperative Association, Rolling Plains Cotton Growers and Central Rolling Plains Co-op Gin. He is a supporter of the Highland FFA and Nolan County Junior Livestock Show.

Asa G. Langford was born in the Lampasas, Texas area in Lampasas County where he currently resides. Mr. Langford is a self-employed rancher whose operation includes a cow-calf herd, stocker cattle, small grains and hay. He, along with his brother, owns an order-buying company, and he also is part owner of a feedlot. Ranching has been his principal occupation for the past five years, and he has been involved in his family's ranch operation for 13 years. He is a graduate of Lampasas High School and earned a BS degree in agricultural economics from Texas A&M University. Mr. Langford is a member of the Lampasas County Farm Bureau and the Texas and Southwestern Cattle Raisers Association. He is a member and deacon of School Creek Baptist Church, and he and his wife Jonna have a son and daughter.

Chad Lee was elected to the Board in 2011 as a Director-Elected Director and serves on the Association's Compensation and Compliance committees. Mr. Lee is a private practice attorney with an emphasis on criminal defense, employment, and various agricultural issues, including contracts and oil and gas leasing and real property disputes. Mr. Lee maintains an operation of commercial cattle, wheat and hay, is a committee member for the Fort Worth Stock Show and Texas Southwestern Cattle Raisers, a Director of Operation Orphans, a non-profit benefiting foster children, and a Director of Tarrant County A&M Club, a non-profit for Aggie Athletics.

Brent Neuhaus was appointed to the Board in 2016 and elected in 2017 and serves on the Association's Audit and Compliance Committees. Mr. Neuhaus lives in Waco, Texas and raises Angus cattle on 243 acres in McLennan County, Texas. Mr. Neuhaus is the Corporate Inventory Manager at United Ag and Turf, which operates John Deere dealerships in Texas, Oklahoma and Arkansas; President and Manager of TGBTG Property, LLC and JORE, LLC, and Member of ERE Property, LLC and HILLRE, LLC, which are involved in real estate. Mr. Neuhaus also has an ownership interest in Neuhaus Trust Partnership through a trust of which he is the trustee, which partnership owns farmland and commercial real estate and other business interests, is a Director and Shareholder of Alliance Bank Central Texas, and is a Director and Chairman of the board of Heart O' Texas Fair & Rodeo. Mr. Neuhaus is married to Kim Neuhaus, who is a first grade teacher in the Midway ISD, and they attend First Woodway Baptist Church.

Bert Pruett was elected to the Board in 1984 and serves on the Association's Audit Committee. Mr. Pruett lives in Slidell in Northwest Denton County, is a self-employed grain farmer, and maintains an operation of cattle, wheat, milo, corn and hay. Mr. Pruett serves as the Treasurer of the Greenwood-Slidell Volunteer Fire Department, President of the Denton-Wise County Farmers Union, and Chairman of the Deacons of the First Baptist Church in Slidell, Texas.

Larry Stewart was elected to the Board in 1984 and serves on the Association's Compensation Committee. Mr. Stewart lives between Granbury and Lipan in Hood County, operates a beef cattle operation as his primary business, and participates in hay production, as well. Mr. Stewart serves as a Director of First National Bank Granbury and as a Director of Hood County Acton Cemetery and previously served as a Director of Cancer Care, which raises money to help cancer victims.

William L. (Bill) Melton has worked for Farm Credit in various capacities for more than 41 years and joined Lone Star Ag Credit on November 08, 2018 as Interim CEO. From February 2017 until October 2018, he served as an Outside Director for Legacy Ag Credit located in Sulphur Springs, Texas. Melton served as the Interim CEO Cape Fear Farm Credit, located in Fayetteville, NC for 2.5 years beginning in July 2013. Until his retirement in June 2013, he served as Senior Vice President and Chief Lending Officer at AgFirst Farm Credit Bank. Prior to joining AgFirst in 1987, Melton was employed for 12 years with three associations located in North Carolina and Georgia and served in roles of increasing responsibility including four years as CEO. He completed a three-year certificate program at the Graduate School of Banking of the South at LSU. He received a B.S. degree in Agricultural Economics from North Carolina State University.

Amy Birt joined the Association in December 2017 as the Chief Financial Officer. Before joining the Association, Ms. Birt served as Chief Financial Officer and Corporate Controller for various commercial financial institutions for over 23 years with expertise in leading the accounting and finance, information technology, human resources, and management information system areas. Ms. Birt, originally from Frankston, Texas, earned her bachelor of business in accounting from Stephen F. Austin State University and her master of accountancy from the University of North Florida. Ms. Birt is a Certified Public Accountant, Chartered Global Management Accountant, and Certified Information Technology Professional.

Sharmyn Calhoun-Alley joined the Association in July 2018 as the Chief Risk Officer. In this role, Ms. Calhoun-Alley leads all aspects of monitoring and compliance; mitigating risk within industry, system and district standards; and supporting sound policy, reporting and governance practices. Prior to joining Lone Star, Ms. Calhoun-Alley served as the Executive Director of Mortgage Compliance and Risk with UBS Bank in Weehawken, NJ. She has successfully created and led compliance and risk management systems in large corporate financial services environments for more than 12 years. Ms. Calhoun-Alley holds degrees from the Indiana University of Pennsylvania for human resource management, as well as computer and office information systems. She also holds a juris doctor from Washburn University School of Law in Topeka, Kansas.

Jeff Davis joined the Association as Chief Operating Officer in September 2018. Before joining the Association, Mr. Davis worked for First Federal Savings & Loan in Port Angeles, WA for four years where he served as Executive Vice President, Chief Operating Officer. Mr. Davis has over 30 years' experience in commercial banking. He earned his bachelor's degree from Indiana Wesleyan University, and master of business administration from Anderson University. He is also a graduate of Stonier Graduate School of Banking.

Jim Bob Reynolds joined the Association in September 2010 as the Senior Vice President of Commercial Credit and now serves as the Chief Credit Officer for the Association. Before joining the Association, Mr. Reynolds worked for First State Bank in Dalhart, Texas for 11 years, where he served as the Senior Vice President of Commercial Lending. Mr. Reynolds is a native of Dalhart, Texas, where he grew up on his family's farming/cattle operation. He earned his bachelor of science degree in ag economics from Texas Tech University and his master of business administration degree from the University of Texas at San Antonio. Jim Bob also attended, graduated from and served on the board of directors of the Rawls College of Business Banking School at Texas Tech University.

COMPENSATION OF DIRECTORS

Directors were compensated for their service to the Association in the form of an honorarium at the rate of $600 per day for director meetings and special meetings, except for the Board Chairman and Vice Chairman, which were compensated at a rate of $1,000 and $800, respectively. The Audit Chairman and Vice Chairman receive an additional honorarium of $500 and $300 per month, respectively. Directors also receive an annual retention fee of $700 per month. Committee meetings that are held in conjunction with another meeting are paid at the rate of $300 per meeting, except for Audit Committee meetings which are paid at the rate of $400 per meeting. Directors are paid an honorarium for conference calls less than an hour at the rate of $200 and for calls in excess of an hour they are compensated $300. Directors were reimbursed for certain expenses incurred while representing the Association in an official capacity. Mileage for attending official meetings during 2018 was paid at the IRS-approved rate of 54.5 cents per mile. A copy of the travel policy is available to stockholders of the Association upon request.

	Number of Days Served		
DIRECTOR	**Board Meeting**	**Other Official Activities**	**2018**
Steven Beakly	7	5	$12,900
Harlin Brown	10	13	$19,400
David Conrad	11	32	$33,000
Don Crawford	12	74	$53,900
Richard Gaona	12	13	$23,200
David Harris	12	61	$42,850
Tom Johnson*	8	52	$34,600
Chad Lee	11	41	$35,150
Brent Neuhaus	12	53	$38,700
Bert Pruett	12	28	$30,800
John Sawyer	12	14	$26,300
Larry Stewart	12	15	$23,100
			$ 373,900

*Mr. Johnson resigned effective October 31, 2018

The aggregate compensation paid to directors in 2018, 2017 and 2016 was $373,900, $365,800 and $301,500, respectively. Additional detail regarding director compensation paid for committee service (which is included in the table above) is as follows:

	Committee			
DIRECTOR	**Audit Committee**	**Compensation Committee**	**Risk Committee**	**Total**
Harlin Brown	$ -	$ 600	$ -	$ 600
David Conrad	4,800	-	400	5,200
Don Crawford	4,800	300	-	5,100
Richard Gaona	1,200	-	-	1,200
David Harris	3,600	300	400	4,300
Tom Johnson*	-	300		300
Chad Lee	-	300	400	700
Brent Neuhaus	4,800	-	-	4,800
Bert Pruett	4,800	-	-	4,800
John Sawyer	-	900	-	900
Larry Stewart	-	600	-	600
	$ 24,000	$ 3,300	$ 1,200	$ 28,500

*Mr. Johnson resigned effective October 31, 2018

The aggregate amount of reimbursement for travel, subsistence and other related expenses paid to directors and on their behalf was $48,826, $96,376 and $113,629 in 2018, 2017 and 2016, respectively.

COMPENSATION OF SENIOR OFFICERS

Compensation Discussion and Analysis – Senior Officers

The objective of the Association's salary administration program is to attract, develop, retain and motivate staff that are knowledgeable and efficient in their ability to support the Association in the execution of its strategic objectives and deliver Association results that maximize the value received by its membership. The Association operates utilizing a compensation program, which focuses on the performance and contributions of its employees in achieving the Association's financial and operational objectives. The Association's Board of Directors, through its Compensation Committee, establishes annual salary and incentive programs utilizing the services of the Human Resources Compensation Team at the Bank to compile "Compensation Market Data" annually that is used by the Board and management in establishing salary levels. Data sources used include the Federal Reserve Bank of Dallas 11th District survey, Texas Community Bank survey (Independent Bankers Association of Texas), Watson Wyatt Financial Institution surveys, Mercer Financial Services Commercial Lending survey and CompData surveys. The Compensation Market Data reveals salary and incentive levels for similar sized institutions operating in our geographic area. Studies provided by third-party compensation specialists form the foundation for the Association's evaluation and establishment of annual salary plans used by the Association. Additional support is provided by an independent outside consultant engaged by the Compensation Committee.

Chief Executive Officer (CEO) Compensation Policy

Name of Individual	Year	Salary (a)	Bonus (b)	Change in Pension Value (c)	Deferred/ Perquisite (d)	Other (e)	Total
William Melton (Interim)	**2018**	**$ 51,706**	**$ -**	**$ -**			**$ 51,706**
Troy Bussmeir	**2018**	**$ 343,343**	**$ -**	**$ -**	**$ 39,991**	**$ 1,244**	**$ 384,578**
CEO	2017	345,013	-	-	57,739	18,354	421,106
	2016	320,012	112,000	-	54,173	26,535	512,720

(a) Gross Salary
(b) Bonuses earned in 2018, 2017 and 2016 were paid in the following year. (No bonus was paid for 2017.)
(c) Change in pension value (noncash)
(d) Deferred Perquisite: 2018, 2017 and 2016 include contribution to 401(k) and defined contribution plans, automobile benefits and premiums paid for life insurance.
(e) Other 2018, 2017 and 2016 includes memberships to professional and social organizations, executive physicals, and travel allowance.

The CEO's salary is established for the period January 1 through December 31 of each year, and is set by the Board using the Compensation Market Data as a guideline to arrive at a fair and competitive salary. The CEO's bonus is at Board discretion and based upon its assessment of the Association's financial performance, credit administration and credit quality goals, and attainment of other goals and objectives specifically established in the Association's Business Plan. This incentive is based on the period from January through December of each year.

Name of Group	Year	Salary (a)	Bonus (b)	Change in Pension Value (c)	Deferred/ Perquisite (d)	Other (e)	Total
Aggregate No. of Senior Officers in Year Excluding CEO							
6	**2018**	**$ 893,776**	**$ 174,126**	**$ -**	**$ 96,579**	**$ 117,519**	**$ 1,282,000**
5	2017	955,275	-	866,921	140,635	336	1,963,167
6	2016	952,273	285,670	675,706	144,194	8,180	2,066,023

(a) Gross Salary
(b) Bonuses earned in 2018, 2017 and 2016 were paid in the following year. (No bonus was paid for 2017)
(c) Change in pension value (noncash)
(d) Deferred Perquisite: 2018, 2017 and 2016 include contribution to 401(k) and defined contribution plans, automobile benefits and premiums paid for life insurance.
(e) Other 2018, 2017 and 2016 includes memberships to professional and social organizations, executive physicals, relocation and travel allowance.

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 is available and will be disclosed to shareholders of the institution upon request.

Employees who use their personal automobile for business purposes were reimbursed during 2018 at the IRS-approved rate of 54.5 cents per mile.

Senior officers, including the CEO, are reimbursed for reasonable travel, subsistence and other related expenses while conducting Association business. A copy of the Association's travel policy is available to shareholders upon request.

No senior officer received non-cash compensation exceeding $5,000, other than that disclosed previously in 2018, 2017 and 2016.

Defined Benefit Pension Plan:

The Defined Benefit Pension Plan (Pension Plan) is a final average pay plan which was closed to new participants in 1996, and later fully closed to all participants, including rehires who had formerly participated in the plan. The Pension Plan benefits are based on the average monthly eligible compensation over the 60 consecutive months that produce the highest average after 1996 ("FAC60"). The Pension Plan's benefit formula for a Normal Retirement Pension is the sum of (a) 1.65 percent of FAC60 times "Years of Benefit Service" and (b) 0.50 percent of (i) FAC60 in excess of Social Security covered compensation times (ii) "Years of Benefit Service" (not to exceed 35).

The Pension Plan's benefit formula for the Normal Retirement Pension assumes that the employee's retirement age is 65, that the employee is married on the date the annuity begins, that the spouse is exactly two years younger than the employee, and that the benefit is payable in the form of a 50 percent joint and survivor annuity. If any of those assumptions are incorrect, the benefit is recalculated to be the actuarial equivalent benefit. The Pension Plan benefit is offset by the pension benefits any employee may have from another Farm Credit System institution.

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 13 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 has 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 on January 1, 2018, or any time during the year just ended.

RELATIONSHIP WITH INDEPENDENT AUDITOR

No change in auditors has taken place since the last annual report to stockholders and no disagreements with auditors have 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 rendered for the Association by PricewaterhouseCoopers LLP for the year ending December 31, 2018 were between $240,000 and $250,000 including $900 for non-audit services and $10,500 for tax services.

FINANCIAL STATEMENTS

The financial statements, together with the report thereon of PricewaterhouseCoopers LLP dated March 13, 2019, and the report of management in this annual report to stockholders, are incorporated herein by reference.

MEMBER/SHAREHOLDER PRIVACY

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

CREDIT AND SERVICES TO YOUNG, BEGINNING AND SMALL FARMERS AND RANCHERS

Lone Star, ACA is obligated to establish programs that respond to the credit and related service needs of Young, Beginning and Small (YBS) farmers and ranchers. It is the Association's responsibility to fulfill its public policy role by extending credit and related services to this important sector of our customer base. YBS farmers and ranchers face continuing challenges in agriculture, including access to capital and credit needs, limited financial resources for land and equipment, urbanization demands and increasing competition from larger and highly capitalized operations.

The Board and management are committed to providing programs that facilitate meeting the needs of this group of customers. These programs also address other issues, including the aging of agricultural landowners and customers, the need to transfer assets to another generation of potential landowners and a recognition that many young, beginning and small operators will need to supplement their farm income by seeking off-farm employment. Additionally, demographic trends indicate that agricultural landowners make decisions regarding land or agricultural endeavors based on lifestyle choices, recreational utility or as an alternative investment in a major financial asset.

Definitions for YBS Farmers and Ranchers

Young Farmer or Rancher- a farmer, rancher or producer/harvester of aquatic products who was age 35 or younger as of the date when the loan was originally made.

Beginning Farmer or Rancher- a farmer, rancher or producer/harvester of aquatic products who had 10 years or less of experience at farming or ranching, or producing or harvesting aquatic products as of the date the loan was originally made.

Small Farmer or Rancher- a farmer, rancher or producer/harvester of aquatic products who normally generates less than $250,000 in annual gross sales of agricultural or aquatic products at the date the loan was originally made.

(A loan to a borrower may meet the definition of an YBS borrower if any one of the categories is achieved.)

In order to address the specific needs of these customers, and to be responsive to the credit needs of young, beginning and small farmers, the Association utilizes all existing loan programs to the maximum benefit of young, beginning and small farmers. The Association has also developed specific loan programs to meet the credit needs of this group. Qualifying young, beginning and small farmers who are involved or becoming more involved in agriculture may be eligible for loans with more flexible rates and fees.

The Association's YBS loans as a percentage of total loans outstanding for years ending 2018, 2017 and 2016, respectively, are reflected in the table below:

	2018		2017		2016	
	% Loans	% Volume	% Loans	% Volume	% Loans	% Volume
Young	17.51	9.79	17.41	9.86	17.72	9.55
Beginning	62.10	50.64	61.13	50.22	59.26	47.28
Small	84.97	61.38	84.51	62.12	82.98	60.99

The Association's YBS loans, as a percentage of all loans closed each year, are reflected in the table below for the past three years:

	2018		2017		2016	
	% Loans	% Volume	% Loans	% Volume	% Loans	% Volume
Young	16.46	8.31	17.95	11.53	17.98	9.22
Beginning	52.36	32.84	59.82	52.14	57.49	43.94
Small	70.85	38.05	80.01	53.92	79.32	59.28

The Board established quantitative targets within the 2018 operational and strategic business plan to measure and evaluate progress toward serving young, beginning and small customers. These volume-based targets for performance included new credit to young farmers at 11.5 percent, to beginning farmers at 55.0 percent, and to small farmers at 62.0 percent. The Board established quantitative targets within the 2018 operational and strategic business plan to measure and evaluate progress toward serving the young, beginning and small customers. These volume-based targets for performance included new credit to young farmers at 11.5 percent. New credit to young and beginning farmers fell short of expectations in 2018, and small farmer achievement was below projected at 38.0 percent. The percentage goals established for small farmers was not achieved primarily due to the level of other loan activity being marginally greater than projected. Goals were also established by the Board for loans outstanding to young, beginning and small farmers. Volume based performance goals for outstanding loans included young borrowers at 10.0 percent, beginning borrowers at 51.0 percent and small borrowers at 64.0 percent of all loans outstanding. Although these goals were not met, results were closer to objectives than was the case of new business, as the overall growth in the loan portfolio outpaced growth in loans to young, beginning, and small farmers.

The United States Department of Agriculture's NASS 2012 Census of Agriculture provides data regarding the actual market for YBS farmers and ranchers within the 48-county area served by Lone Star. This census data indicated 8.0 percent of farm operators are "young," 30.4 percent of operators are "beginning" and 97.5 percent of farm units are categorized as "small." There are differences in the method by which Association YBS data and demographic census data is described. Census data is based on the number of farms, and Association data is based on the number of customers. Additionally, census dates do not coincide with an annual analysis of Association data, and calculations for young and beginning farmers are slightly different. Annual performance data and goals established also include lending activity outside the Association's territory. However, a comparison does offer a quantitative measure of the Association's performance in fulfilling its mission of service to young, beginning and small farmers.

The Association coordinates its young, beginning and small farmer loan program activities with other lenders. This includes the purchase and sale of loan participations, loan guarantees and joint lending. Related services including appraisal, credit life insurance, life and disability products and leasing programs are available to assist YBS borrowers in their credit and related service needs.

Important components of the Association's YBS efforts include the emphasis placed on outreach programs. The Association has held a long-standing belief that an investment in agricultural students and youth activities is important to the long-term success of the cooperative. The Association develops a comprehensive array of marketing efforts to include youth activities and events including livestock shows, 4-H and FFA events, young professional groups and agricultural leadership opportunities.

The Association offers a scholarship program for area seniors and four scholarships are awarded in the lending area. The Association also sponsors youth activities in the local area and at the state level through support of 4-H and FFA activities.

A YBS Advisory Board was formed to generate ideas and methods on how Lone Star, ACA can better serve the YBS demographic in our area. The advisory board minutes are reported to the Board.

In summary, the Association fulfills its mission of providing agricultural credit and meeting the specific credit and related service needs of young, beginning and small farmers, ranchers and producers/harvesters of aquatic products through specific lending programs, quantitative performance measures and broad-based objectives.