CoBank Quarterly District Financial Information September 30, 2018

Quarterly District Financial Information

CoBank, ACB and Affiliated Associations

Introduction and District Overview

CoBank, ACB (CoBank, the Bank, we, our, or us) is one of the four banks of the Farm Credit System (System) and provides loans, leases and other financial services to support agriculture, rural infrastructure and rural communities across the United States. The System is a federally chartered network of borrower-owned lending institutions composed of cooperatives and related service organizations. The System was established in 1916 by the U.S. Congress, and is a Government Sponsored Enterprise. CoBank is federally chartered under the Farm Credit Act of 1971, as amended (the Farm Credit Act), and is subject to supervision, examination, and safety and soundness regulation by an independent federal agency, the Farm Credit Administration (FCA).

We are cooperatively owned by our U.S. customers. Our customers consist of agricultural cooperatives; other food and agribusiness companies; rural power, communications and water cooperatives and companies; rural community facilities; Agricultural Credit Associations (Associations), which are regulated, farmer-owned financial institutions and members of the System; and other businesses that serve agriculture and rural communities. The Associations originate and service long-term real estate mortgage loans as well as short- and intermediate-term loans for agricultural and other purposes to full and part-time farmers. Associations may also make loans to, among others, processing and marketing entities, farm-related businesses, and rural residents for home purchase and improvement. The Associations may also purchase eligible loan participations from System entities and other lending institutions. Additionally, the Associations serve as an intermediary in offering multi-peril crop insurance and credit life insurance, and providing additional financial services to borrowers.

We are chartered by the FCA to serve the Associations that provide credit and related financial services to or for the benefit of eligible borrowers/shareholders for qualified purposes in specific geographic areas in the United States. We collectively refer to these entities as our affiliated Associations. Associations do not participate in the issuance of Systemwide bonds, medium term notes and discount notes (collectively referred to as Systemwide Debt Securities). Therefore, we are the primary funding source for our affiliated Associations. As of September 30, 2018, we have 22 affiliated Associations serving customers in 23 states across the Northwest, West, Southwest, Rocky Mountains, Mid-Plains, and Northeast regions of the United States.

Our affiliated Associations are considered customers and thus operate independently and maintain an arms-length relationship with us, except to the extent that the Farm Credit Act requires us, as the funding bank, to monitor and approve certain activities of these Associations. Accordingly, the financial information of affiliated Associations is not included in the condensed consolidated quarterly financial statements presented in CoBank's September 30, 2018 Quarterly Report to Shareholders. However, because of the interdependent manner in which CoBank and our affiliated Associations operate, we believe that presenting combined Bank and Association quarterly financial information could be meaningful for purposes of additional analysis.

The Financial Highlights, Discussion and Analysis, and the Condensed Combined Balance Sheets and Statements of Income included on the following pages present unaudited combined financial information and related analysis of CoBank and its affiliated Associations, which are collectively referred to as the "District." As part of the combining process, all significant transactions between CoBank and the Associations, including loans made by the Bank to the affiliated Associations and the interest income/interest expense related thereto, and investments of the affiliated Associations in the Bank and the earnings related thereto, have been eliminated.

Quarterly District Financial Information
CoBank, ACB and Affiliated Associations

Financial Highlights

($ in Thousands) (Unaudited)

	September 30, 2018	December 31, 2017
Total Loans	**$ 108,929,271**	$ 109,377,684
Less: Allowance for Loan Losses	**906,297**	884,027
Net Loans	**108,022,974**	108,493,657
Total Assets	**139,548,897**	140,234,801
Total Shareholders' Equity	**19,252,225**	18,432,074

For the Nine Months Ended September 30,	2018	2017
Net Interest Income	**$ 2,245,177**	$ 2,139,309
Provision for Loan Losses	**55,840**	55,431
Net Fee Income	**101,589**	100,937
Net Income	**1,658,010**	1,369,075
Net Interest Margin	**2.12 %**	2.11 %
Return on Average Assets	**1.55**	1.33
Return on Average Total Shareholders' Equity	**11.72**	10.15
Average Loans	**$ 110,821,194**	$ 105,720,781
Average Earning Assets	**141,102,358**	135,134,307
Average Assets	**142,790,395**	136,832,505

Discussion and Analysis of District Results of Operations and Financial Condition

District average loan volume increased 5 percent to $110.8 billion in the first nine months of 2018, compared to $105.7 billion for the same period of 2017. The increase in average loan volume primarily reflected growth in agribusiness and real estate mortgage loans.

District net income increased $288.9 million to $1,658 million for the nine-month period ended September 30, 2018, compared to $1,369 million for the same period of 2017. The increase in earnings primarily resulted from increases in noninterest income and net interest income as well as a lower provision for income taxes and a decrease in operating expenses. The increase in noninterest income was largely due to a return of excess insurance funds from the Farm Credit System Insurance Corporation (Insurance Corporation) as well as a higher level of gains on the sale of investment securities and lower losses on early extinguishments of debt at CoBank.

Net interest income increased $105.9 million to $2,245 million for the first nine months of 2018 from $2,139 million for the same period in 2017. The increase in net interest income was primarily driven by growth in average loan volume. The District's overall net interest margin increased to 2.12 percent for the nine months ended September 30, 2018, from 2.11 percent for the same period in 2017. The improvement in net interest margin for the first nine months of 2018 primarily reflected a higher level of lending to grain and farm supply customers in CoBank's agribusiness operating segment as well as increased earnings on invested capital as compared to the 2017 period.

The District recorded a provision for loan losses of $55.8 million in the nine-month period ended September 30, 2018, compared to $55.4 million for the same period of 2017. CoBank recorded a provision for loan losses of $43.0 million in the first nine months of 2018 compared to $38.0 million during the 2017 period. The 2018 provision at CoBank largely reflected increases in specific reserves associated with a small number of customers as well as increased exposure in CoBank's agribusiness loan portfolio resulting from deterioration in credit quality and growth in average loan volume. The Associations recorded a net combined provision for loan losses of $12.8 million for the first nine months of 2018, compared to a net combined provision of $17.4 million in the same period of 2017. The net combined 2018 and 2017 provisions for loan losses at the Associations were primarily due to provisions at several Associations resulting from deterioration in credit quality and other concerns causing stress to specific industries.

Noninterest income increased $143.5 million to $345.3 million for the first nine months of 2018 from $201.8 million for the same period in 2017. Noninterest income is primarily composed of fee income, patronage income, loan prepayment income and miscellaneous gains and losses, offset by losses on early extinguishments of debt. The increase in noninterest income resulted largely from the return of $69.5 million in excess insurance funds from the Insurance Corporation related to the Farm Credit Insurance Fund (Insurance Fund). When the Insurance Fund exceeds the statutory 2 percent secure base amount (SBA), the Insurance Corporation is required to reduce premiums and may return excess amounts. The Insurance Fund began 2018 above the SBA. In the first quarter of 2018, the Insurance Corporation approved the distribution of the excess amounts and such amounts were distributed to System entities in March. The increase in noninterest income was also driven by a higher level of gains recognized on the sale of investment securities. In the first nine months of 2018, CoBank sold investment securities with a combined book value of $1.4 billion for gains totaling $49.0 million. During the nine-month period ended September 30, 2017, CoBank sold investment securities with a combined book value of $1.6 billion for gains totaling $9.4 million. Losses on early extinguishments of debt, net of prepayment income, decreased $30.4 million during the nine months ended September 30, 2018, compared to the same prior-year period as CoBank took advantage of market opportunities to buy back significantly more high cost debt in the 2017 period. While it is the Bank's general practice to extinguish debt to offset the current and prospective impact of prepayments in the loan and investment portfolios, the availability in the market of similarly-tenored debt, coupled with the timing of prepayments, do not always allow us to fully offset the impact of prepayments. The increase in other noninterest income in 2018 also included gains on the disposition of warrants which had been obtained by CoBank and several Associations in a previous loan restructuring. Patronage income, which represents patronage received from other System institutions on loan participations sold by CoBank and two other Associations, increased $7.4 million in the first nine months of 2018 compared to the 2017 period.

District operating expenses decreased $4.1 million to $797.1 million in the first nine months of 2018 from $801.2 million for the same period of 2017. The lower level of operating expenses was driven by a decrease in Insurance Fund premium expense of $39.8 million in the first nine months of 2018 compared to the 2017 period. The decrease is due to the impact of lower premium rates partially offset by higher levels of insured debt obligations to fund growth in loan volume. Insurance Fund premium rates are set by the Insurance Corporation and were 9 basis points of adjusted insured debt obligations in the first nine months of 2018 compared to 15 basis points during the 2017 period. The Insurance Corporation announced that the premium rate will remain at 9 basis points of average outstanding adjusted insured debt for the remainder of 2018. This item was somewhat offset by an increase in other operating expenses of $11.7 million resulting primarily from a change in the classification of certain components of pension expenses due to accounting guidance which was adopted in 2018. Employee compensation expense increased by $8.3 million in the nine months ended September 30, 2018. The increase in employee compensation was primarily driven by annual merit increases and a higher overall number of employees in the first nine months of 2018 compared to the same period in 2017, somewhat offset by the reclassification of certain pension expenses to other operating expenses, as mentioned above. Information services expense increased $6.2 million in the nine months ended September 30, 2018 compared to the 2017 period primarily due to greater expenditures at CoBank and certain Associations to enhance service offerings and technology platforms. Occupancy and equipment expenses increased by $4.0 million primarily due to higher costs relating to improvements and maintenance at several Associations. Purchased services increased by $3.3 million primarily due to strategic initiatives at several Associations.

Income tax expense decreased $35.9 million for the nine-month period ended September 30, 2018, compared to the same period of 2017. The income tax expense at the District predominantly relates to CoBank, as a substantial majority of the business activities at Associations are exempt from federal income tax. The decrease in income tax expense was primarily due to the enactment of federal tax legislation in late 2017 which, among other things, lowered the federal corporate tax rate from 35 percent to 21 percent beginning in 2018. This decrease included a $16.0 million tax benefit recorded during the second quarter of 2018 which resulted from a change in accounting estimate reflecting the full effects of the enactment of federal tax legislation on CoBank's 2017 income tax provision. A higher level of tax-deductible patronage at CoBank, driven by the special patronage distribution described on page 11, also contributed to the decrease in income tax expense during the nine-month period ended September 30, 2018.

Loan Portfolio

The following table presents the District's outstanding loans classified in accordance with the FCA's loan types.

($ in Thousands)

District Loans by Loan Type

	September 30, 2018	December 31, 2017
Real Estate Mortgage	**$ 33,595,427**	$ 32,344,144
Non-affiliated Associations	**4,872,789**	4,859,323
Production and Intermediate-term	**15,269,415**	15,306,715
Agribusiness:		
Loans to Cooperatives	**12,310,325**	14,565,105
Processing and Marketing Operations	**8,531,068**	8,179,923
Farm-Related Businesses	**1,754,895**	1,600,016
Communications	**3,971,209**	4,086,271
Rural Power	**16,576,436**	16,658,551
Water/Waste Water	**1,879,211**	1,767,950
Agricultural Export Finance	**5,600,771**	5,268,391
Rural Residential Real Estate	**784,349**	848,362
Lease Receivables	**3,669,712**	3,761,678
Other	**113,664**	131,255
Total	**$ 108,929,271**	$ 109,377,684

Overall District loan volume decreased $0.5 billion to $108.9 billion at September 30, 2018, as compared to loan volume as of December 31, 2017. The decrease was primarily due to lower seasonal loan volume in CoBank's agribusiness portfolio, which typically reaches a low in late summer or early fall. This decrease was largely offset by increases in real estate mortgage loans at Associations as well as processing and marketing operations and agricultural export finance loans at CoBank.

Loan Quality

The following table presents loans, classified by management at the various District entities pursuant to the FCA's Uniform Loan Classification System, as a percent of total loans.

District Loan Quality

	September 30, 2018	December 31, 2017
Acceptable	**94.13 %**	94.35 %
Special Mention	**3.13**	3.20
Substandard	**2.72**	2.44
Doubtful	**0.02**	0.01
Loss	**-**	-
Total	**100.00 %**	100.00 %

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While our overall loan quality within the District remains favorable, certain entities within the District, including CoBank, experienced credit quality deterioration in the first nine months of 2018 resulting from commodity price volatility and other concerns causing stress to specific industries. Acceptable loans and accrued interest decreased to 94.13 percent at September 30, 2018, compared to 94.35 percent at December 31, 2017. The level of adversely classified loans ("Substandard", "Doubtful" and "Loss") as a percent of total loans was 2.74 percent at September 30, 2018, compared to 2.45 percent at December 31, 2017. These movements were primarily driven by deterioration in credit quality impacting agribusiness, real estate mortgage as well as short and intermediate-term loans.

At September 30, 2018, Special Mention loans included a CoBank participation in a $471.1 million wholesale loan made by Farm Credit Bank of Texas to one of its affiliated Associations. Pursuant to regulatory requirements, wholesale loans are classified using the same credit rating methodology as is used with commercial loans. Our loans to Associations are collateralized by substantially all of the Association assets. In addition, the earnings, capital and loan loss reserves of the Associations provide additional layers of protection against losses in their retail loan portfolios. While the downgrade reflects certain material internal control weaknesses at that Association, as a result of the collateralization and other mitigants described above, no losses are anticipated related to that wholesale loan. As of September 30, 2018, CoBank has not made any provision for loan loss or recorded any allowance for credit loss related to any wholesale loans to Associations.

Credit risk in the District's loan portfolio is spread broadly among customers, industries and geographic territory. The District serves a diversified spectrum of borrowers up and down the agricultural value chain. Association retail loans in the District loan portfolio are concentrated in the Northwest, West, Southwest, Rocky Mountains, Mid-Plains, and Northeast regions of the United States. CoBank's commercial loan portfolio extends across the United States, with moderate levels of concentration in the Midwest region of the country and in the farm supply, grain marketing, electric distribution, and generation and transmission sectors.

Nonperforming assets (which consist of nonaccrual loans, accruing restructured loans, accruing loans 90 days or more past due and other property owned) totaled $856.6 million as of September 30, 2018, compared to $614.5 million at December 31, 2017. Nonaccrual loans increased by $242.0 million during the first nine months of 2018. Nonaccrual loans at CoBank increased by $131.0 million primarily resulting from credit quality deterioration impacting a small number of agribusiness and rural power customers. Nonaccrual loans at Associations increased by $111.0 million primarily due to the addition of several agribusiness, production and intermediate-term and real estate mortgage loans to nonaccrual status during 2018. Accruing restructured loans decreased by $7.5 million to $33.0 million in the nine-month period ended September 30, 2018 primarily due to payoff activity at two Associations. Total accruing loans 90 days or more past due increased by $12.3 million during the first nine months of 2018 primarily driven by increases at four Associations. Nonperforming assets represented 0.79 percent of total District loan volume and other property owned at September 30, 2018, compared to 0.56 percent at December 31, 2017. Nonaccrual loan volume, the largest component of nonperforming assets, represented 0.73 percent of total loans at September 30, 2018, compared to 0.51 percent of total loans at December 31, 2017.

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The following table displays the District's nonperforming assets for the periods presented.

($ in Thousands)

Nonperforming Assets	September 30, 2018	December 31, 2017
Nonaccrual Loans:		
Real Estate Mortgage	$ **238,488**	$ 227,649
Production and Intermediate-term	**127,821**	100,681
Agribusiness	**339,355**	141,838
Communications	**9,798**	10,639
Rural Power	**29,259**	23,218
Agricultural Export Finance	**-**	4,091
Rural Residential Real Estate	**3,637**	2,013
Lease Receivables	**47,570**	43,755
Total Nonaccrual Loans	**795,928**	553,884
Accruing Restructured Loans:		
Real Estate Mortgage	**18,960**	19,607
Production and Intermediate-term	**11,967**	18,700
Agribusiness	**-**	21
Rural Residential Real Estate	**2,116**	2,174
Total Accruing Restructured Loans	**33,043**	40,502
Accruing Loans 90 Days or More Past Due:		
Real Estate Mortgage	**12,876**	1,723
Production and Intermediate-term	**6,153**	1,416
Agribusiness	**509**	3,526
Rural Residential Real Estate	**51**	723
Lease Receivables	**738**	670
Total Accruing Loans 90 Days or More Past Due	**20,327**	8,058
Total Nonperforming Loans	**849,298**	602,444
Other Property Owned	**7,299**	12,062
Total Nonperforming Assets	$ **856,597**	$ 614,506
Nonaccrual Loans as a Percentage of Total Loans	**0.73 %**	0.51 %
Nonperforming Assets as a Percentage of Total Loans and Other Property Owned	**0.79**	0.56
Nonperforming Assets as a Percentage of Capital	**4.45**	3.33

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The following tables present an aging of past due loans in the District for the periods presented.

($ in Thousands)

Aging of Past Due Loans

	September 30, 2018					
	30-90 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans and Accrued Interest	Recorded Investment >90 Days and Accruing
Real Estate Mortgage	$ 95,913	$ 126,467	$ 222,380	$ 33,919,198	$ 34,141,578	$ 12,876
Production and Intermediate-term	50,157	85,741	135,898	15,286,831	15,422,729	6,153
Agribusiness	17,391	9,959	27,350	22,664,188	22,691,538	509
Communications	-	-	-	3,981,743	3,981,743	-
Rural Power	-	21,832	21,832	16,630,488	16,652,320	-
Water/Waste Water	-	-	-	1,889,065	1,889,065	-
Agricultural Export Finance	-	-	-	5,625,583	5,625,583	-
Rural Residential Real Estate	5,244	1,571	6,815	780,334	787,149	51
Lease Receivables	10,446	16,795	27,241	3,643,339	3,670,580	738
Non-affiliated Associations	-	-	-	4,883,874	4,883,874	-
Other	79	-	79	113,902	113,981	-
Total	$ 179,230	$ 262,365	$ 441,595	$ 109,418,545	$ 109,860,140	$ 20,327

($ in Thousands)

Aging of Past Due Loans

	December 31, 2017					
	30-90 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans and Accrued Interest	Recorded Investment >90 Days and Accruing
Real Estate Mortgage	$ 64,345	$ 80,065	$ 144,410	$ 32,559,239	$ 32,703,649	$ 1,723
Production and		-				
Intermediate-term	51,053	62,384	113,437	15,306,173	15,419,610	1,416
Agribusiness	7,062	12,639	19,701	24,417,410	24,437,111	3,526
Communications	2	-	2	4,099,011	4,099,013	-
Rural Power	-	-	-	16,730,893	16,730,893	-
Water/Waste Water	-	-	-	1,778,048	1,778,048	-
Agricultural Export Finance	-	-	-	5,283,839	5,283,839	-
Rural Residential Real Estate	6,856	1,377	8,233	842,857	851,090	723
Lease Receivables	41,406	7,591	48,997	3,713,481	3,762,478	670
Non-affiliated Associations	-	-	-	4,867,557	4,867,557	-
Other	79	-	79	131,497	131,576	-
Total	$ 170,803	$ 164,056	$ 334,859	$ 109,730,005	$ 110,064,864	$ 8,058

Quarterly District Financial Information

CoBank, ACB and Affiliated Associations

District entities maintain an allowance for loan losses at a level consistent with the probable losses identified by management of each institution, considering such factors as current agricultural and economic conditions, loan loss experience, portfolio quality, and loan portfolio composition and concentrations. CoBank and certain Associations also maintain a reserve for unfunded commitments, which totaled $141.4 million at September 30, 2018.

Although aggregated in the District's condensed combined financial statements, the allowance for loan losses for each District entity is particular to that institution and is not available to absorb losses realized by other District entities. The allowance for loan losses at September 30, 2018 totaled $906.3 million compared to $884.0 million at December 31, 2017. Changes in the allowance during the first nine months of 2018 included an overall provision for loan losses of $55.8 million, which is described on page 3, loan charge-offs of $32.9 million, a $6.9 million net transfer to the reserve for unfunded commitments, and loan recoveries of $6.2 million.

The following tables present detailed changes in the allowance for loan losses in the District for the periods presented.

($ in Thousands)

Changes in Allowance for Loan Losses

	Balance at December 31, 2017	Charge-offs	Recoveries	Provision for Loan Losses/ (Loan Loss Reversal)	Transfers from/(to) Reserve for Unfunded Commitments	Balance at September 30, 2018
Real Estate Mortgage	$ 127,851	$ (3,060)	$ 1,891	$ 3,550	$ 1,382	$ 131,614
Production and Intermediate-term	170,997	(3,737)	2,836	14,122	(1,885)	182,333
Agribusiness	343,003	(21,724)	865	26,043	(11,636)	336,551
Communications	50,189	-	52	5,144	288	55,673
Rural Power	112,042	(2,135)	201	(87)	4,438	114,459
Water/Waste Water	11,606	-	-	433	486	12,525
Agricultural Export Finance	16,403	-	117	1,496	78	18,094
Rural Residential Real Estate	3,673	(13)	-	(303)	-	3,357
Lease Receivables and Other	48,263	(2,234)	228	5,442	(8)	51,691
Total	$ 884,027	$ (32,903)	$ 6,190	$ 55,840	$ (6,857)	$ 906,297

($ in Thousands)

Changes in Allowance for Loan Losses

	Balance at December 31, 2016	Charge-offs	Recoveries	Provision for Loan Losses/ (Loan Loss Reversal)	Transfers (to)/from Reserve for Unfunded Commitments	Association Merger Impact	Balance at September 30, 2017
Real Estate Mortgage	$ 125,268	$ (743)	$ 270	$ 7,174	$ (5,811)	$ (1,156)	$ 125,002
Production and Intermediate-term	156,333	(5,182)	2,442	27,874	(2,669)	(1,731)	177,067
Agribusiness	336,588	(1,565)	849	13,928	(14,915)	(242)	334,643
Communications	40,564	-	45	(318)	1,035	(25)	41,301
Rural Power	124,026	-	170	567	(1,695)	(85)	122,983
Water/Waste Water	11,724	-	-	1,135	(176)	(4)	12,679
Agricultural Export Finance	14,216	-	420	1,035	30	(8)	15,693
Rural Residential Real Estate	4,497	(219)	35	(658)	-	(2)	3,653
Lease Receivables and Other	42,103	(1,795)	104	4,694	-	-	45,106
Total	$ 855,319	$ (9,504)	$ 4,335	$ 55,431	$ (24,201)	$ (3,253)	$ 878,127

District Capital Resources and Other

Combined District shareholders' equity at September 30, 2018 totaled $19.3 billion, a net increase of $820.2 million as compared to December 31, 2017. The increase primarily resulted from District net income of $1,658 million, an increase in common stock of $55.5 million and an increase in preferred stock at Associations of $25.4 million. These items were partially offset by an increase in accrued patronage of $465.1 million, driven by the special patronage distribution at CoBank described on page 11, as well as increases in accumulated other comprehensive loss of $407.1 million and preferred stock dividends of $73.5 million.

The components of the District's accumulated other comprehensive loss are detailed in the following table.

($ in Thousands)

Accumulated Other Comprehensive Loss

	September 30, 2018	December 31, 2017
Unrealized Losses on Investment Securities	**$ (565,182)**	$ (121,149)
Net Pension Adjustment	**(342,987)**	(351,097)
Unrealized Losses on Interest Rate Swaps and Other Financial Instruments	**(21,121)**	(49,981)
Accumulated Other Comprehensive Loss	**$ (929,290)**	$ (522,227)

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The increase in the District's total accumulated other comprehensive loss during the first nine months of 2018 is primarily due to an increase in unrealized losses on investment securities at CoBank driven by market interest rate changes. Also contributing to the increased loss was the reclassification of certain stranded tax effects totaling $26.8 million. New U.S. tax laws resulting from legislation commonly known as the Tax Cuts and Jobs Act of 2017 (TCJA) were enacted in late 2017. Among other things, the TCJA reduced the federal corporate tax rate from 35 percent to 21 percent. In accordance with accounting principles generally accepted in the United States of America (GAAP), the change to a lower corporate tax rate led to a remeasurement of deferred tax liabilities and deferred tax assets in the period of enactment (2017). For deferred tax amounts originally recorded in accumulated other comprehensive income/(loss), this remeasurement resulted in a disproportionate effect of $26.8 million for the District which remained "stranded" in accumulated other comprehensive loss as of December 31, 2017. In February 2018, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU), "Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income." The new guidance provides entities the option to reclassify the stranded tax effects of the TCJA from accumulated other comprehensive income/(loss) to retained earnings. For all entities, this guidance becomes effective for financial statements issued for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. The District elected to early adopt this guidance, as permitted by the standard. As a result, the stranded tax effect was reclassified at the beginning of 2018 resulting in increases to accumulated other comprehensive loss and retained earnings of $26.8 million.

In September 2018, CoBank made a special all-cash patronage distribution of $96.2 million to customer-owners. The distribution reflects CoBank's plan to share the benefits of recently enacted federal tax reform legislation with eligible borrowers and other key stakeholders, along with earnings from significant nonrecurring items in 2018. The distribution was incremental to standard patronage distributions that CoBank typically makes in March of each year.

The following tables present regulatory capital and leverage ratios for CoBank and the range of ratios at the affiliated Associations.

Regulatory Capital and Leverage Ratios

As of September 30, 2018

	Common Equity Tier 1 Capital Ratio	Tier 1 Capital Ratio	Total Capital Ratio	Tier 1 Leverage Ratio	Unallocated Retained Earnings (URE) and URE Equivalents Leverage Ratio	Permanent Capital Ratio
CoBank	12.60 %	14.86 %	15.92 %	7.65 %	3.25 %	14.99 %
Calculated Buffer	8.10	8.86	7.92	3.65	n/a	n/a
Associations	13.80 - 28.04	13.80 - 28.04	14.22 - 29.30	14.43 - 26.80	16.78 - 26.42	13.99 - 31.77
Calculated Buffers	9.30 - 23.54	7.80 - 22.04	6.22 - 21.30	10.43 - 22.80	n/a	n/a
Regulatory Minimum	4.5	6.0	8.0	4.0	1.5	7.0
Required Buffer	2.5 (1)	2.5 (1)	2.5 (1)	1.0	n/a	n/a

(1) The capital conservation buffer will be phased in over three years, reaching its full value of 2.5 percent in 2020.

Regulatory Capital and Leverage Ratios
As of December 31, 2017

	Common Equity Tier 1 Capital Ratio	Tier 1 Capital Ratio	Total Capital Ratio	Tier 1 Leverage Ratio	Unallocated Retained Earnings (URE) and URE Equivalents Leverage Ratio	Permanent Capital Ratio
CoBank	11.67 %	13.97 %	15.24 %	7.26 %	2.96 %	14.29 %
Calculated Buffer	7.17	7.97	7.24	3.26	n/a	n/a
Associations	13.33 - 29.45	13.33 - 29.45	13.95 - 30.70	14.37 - 27.50	15.99 - 27.10	14.30 - 33.32
Calculated Buffers	8.83 - 24.95	7.33 - 23.45	5.95 - 22.70	10.37 - 23.50	n/a	n/a
Regulatory Minimum	4.5	6.0	8.0	4.0	1.5	7.0
Required Buffer	2.5 (1)	2.5 (1)	2.5 (1)	1.0	n/a	n/a

(1) The capital conservation buffer will be phased in over three years, reaching its full value of 2.5 percent in 2020.

As depicted in the tables above, at September 30, 2018, CoBank and all affiliated Associations exceeded the FCA's regulatory minimum capital ratios and any required buffers. Although aggregated in the District's condensed combined financial statements, capital for each District entity is particular to that institution. In addition, the provisions of joint and several liability for Systemwide Debt Securities are applicable only to System banks and do not include Associations. CoBank has no access to Association capital beyond their required investment in the Bank. There are no capital sharing agreements between CoBank and its affiliated Associations.

Other Matters

In June 2016, a lawsuit was commenced by the filing of a complaint in the United States District Court Southern District of New York against CoBank by a number of investors (the "Plaintiffs") who had held CoBank's 7.875 percent Subordinated Notes due in 2018 (the "Notes"). The Notes were redeemed at par plus accrued interest by CoBank in April 2016 due to the occurrence of a "Regulatory Event" (as defined under the terms of the Notes). The Plaintiffs have asserted a breach of contract claim and a breach of implied covenant of good faith and fair dealing claim alleging that CoBank impermissibly redeemed the Notes. The Plaintiffs have requested damages in an amount to be determined at trial, reasonable attorneys' fees and any other such relief as the court may deem just and proper. CoBank filed its answer in September 2016 and discovery concluded in January 2018. CoBank and Plaintiffs filed their respective motions for summary judgment in March 2018. There is presently no indication of when the court will rule on the motions for summary judgment. CoBank intends to vigorously defend against these allegations. The likelihood of any outcome of this proceeding cannot be determined at this time.

Quarterly District Financial Information

CoBank, ACB and Affiliated Associations

Condensed Combined Balance Sheets

(unaudited)

($ in Thousands)

	September 30, 2018	December 31, 2017
Assets		
Total Loans	**$ 108,929,271**	$ 109,377,684
Less: Allowance for Loan Losses	**906,297**	884,027
Net Loans	**108,022,974**	108,493,657
Cash and Cash Equivalents	**291,640**	1,548,892
Federal Funds Sold and Other Overnight Funds	**426,000**	1,035,000
Investment Securities	**28,415,898**	26,980,570
Interest Rate Swaps and Other Financial Instruments	**256,281**	171,148
Accrued Interest Receivable and Other Assets	**2,136,104**	2,005,534
Total Assets	**$ 139,548,897**	$ 140,234,801
Liabilities		
Bonds and Notes	**$ 118,132,817**	$ 119,386,740
Interest Rate Swaps and Other Financial Instruments	**195,059**	86,732
Reserve for Unfunded Commitments	**141,444**	134,587
Accrued Interest Payable and Other Liabilities	**1,827,352**	2,194,668
Total Liabilities	**120,296,672**	121,802,727
Shareholders' Equity		
Preferred Stock Issued by Bank	**1,500,000**	1,500,000
Preferred Stock Issued by Associations	**558,090**	532,649
Common Stock	**1,596,814**	1,541,275
Paid In Capital	**1,319,232**	1,319,232
Unallocated Retained Earnings	**15,207,379**	14,061,145
Accumulated Other Comprehensive Loss	**(929,290)**	(522,227)
Total Shareholders' Equity	**19,252,225**	18,432,074
Total Liabilities and Shareholders' Equity	**$ 139,548,897**	$ 140,234,801

Quarterly District Financial Information
CoBank, ACB and Affiliated Associations

Condensed Combined Statements of Income
(unaudited)

($ in Thousands)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2018	**2017**	**2018**	**2017**
Interest Income				
Loans	**$ 1,231,519**	$ 1,034,212	**$ 3,608,951**	$ 3,005,725
Investment Securities, Federal Funds Sold and Other Overnight Funds	**174,857**	140,319	**506,017**	401,901
Total Interest Income	**1,406,376**	1,174,531	**4,114,968**	3,407,626
Interest Expense	**666,657**	461,524	**1,869,791**	1,268,317
Net Interest Income	**739,719**	713,007	**2,245,177**	2,139,309
Provision for Loan Losses	**13,108**	28,105	**55,840**	55,431
Net Interest Income After Provision for Loan Losses	**726,611**	684,902	**2,189,337**	2,083,878
Noninterest Income/(Expense)				
Net Fee Income	**43,183**	32,090	**101,589**	100,937
Patronage Income	**15,582**	14,653	**57,852**	50,430
Prepayment Income	**12,097**	6,646	**15,312**	13,473
Losses on Early Extinguishments of Debt	**(3,550)**	(31,615)	**(9,447)**	(37,981)
Gains on Sale of Investment Securities	**8,439**	-	**48,998**	9,387
Return of Excess Insurance Funds	**-**	-	**69,504**	-
Other, Net	**7,974**	19,313	**61,469**	65,521
Total Noninterest Income	**83,725**	41,087	**345,277**	201,767
Operating Expenses				
Employee Compensation	**152,787**	148,603	**450,549**	442,213
Insurance Fund Premium	**21,477**	34,900	**66,458**	106,220
Information Services	**18,806**	17,462	**56,988**	50,763
General and Administrative	**17,539**	16,257	**54,028**	52,431
Occupancy and Equipment	**19,334**	17,404	**51,724**	47,682
Farm Credit System Related	**6,862**	6,903	**23,667**	23,102
Purchased Services	**16,471**	13,727	**45,051**	41,786
Other	**16,115**	12,101	**48,666**	37,000
Total Operating Expenses	**269,391**	267,357	**797,131**	801,197
Income Before Income Taxes	**540,945**	458,632	**1,737,483**	1,484,448
Provision for Income Taxes	**17,251**	29,402	**79,473**	115,373
Net Income	**$ 523,694**	$ 429,230	**$ 1,658,010**	$ 1,369,075