2016 Annual Report

Welcoming Our Ninth Decade

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Letter from the Chairman

This year's report is a lookback at our rich history of over 80 years, where we are today and how we are positioning ourselves for a long and fulfilling future. All the many achievements are a testament to the Credit Union staff that makes banking at your Credit Union a unique and rewarding experience. I am especially proud of what we have held true over these 80 years of growth: we've never lost sight of what really matters, working together to enrich the lives of our members, and helping each other out as only family does. In a world defined so much by numbers and targets, this is a fine legacy – the bond that we have created with our Farmers family.

I am also pleased to say that our Credit Union experienced another successful year in the areas of growth, quality, productivity, and profitability; even in the face of the most significant and demanding series of technology upgrades in our history, all designed to improve our responsiveness and member service. These upgrades were not without frustrating problems that tested everyone's mettle. We did, however, emerge a stronger organization – and with our enhanced capabilities will deliver a better member banking experience in 2017 and beyond. I owe our members a large debt of gratitude for their patience through this challenging period, and proudly applaud the phenomenal work and resolve of our Credit Union staff.

On behalf of the Board of Directors, I want to thank management and staff for their dedication and service. The Credit Union achieved gross income of $46,425,000 and net income of $6,062,000. We continued to grow net worth to 14% and assets to $712,400,000. As a result, the Credit Union was able to return almost $2 million to members in the form of cash dividends, loan rebates and higher dividend rates. These earnings would normally go back to stockholders at a for-profit institution, but because our Credit Union is not-for-profit, we were able to give it back to our valued members...to our *family*.

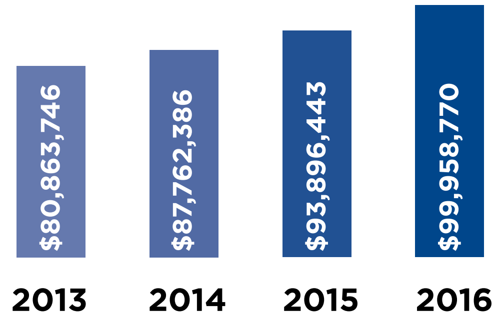
Ultimately, our Credit Union members make all of our accomplishments possible, and I would like to thank you, our member-owners, for your membership and support. Our Credit Union exists solely to enhance our members' financial lives, and we cannot grow and prosper without your active participation. As we look forward to the next 80 years and build our financial services and product offerings, we will continue to focus on the care and service that makes us unique. We will never lose sight of our commitment to you. After all, we are *family*.

Scott Lindquist, Chairman of the Board

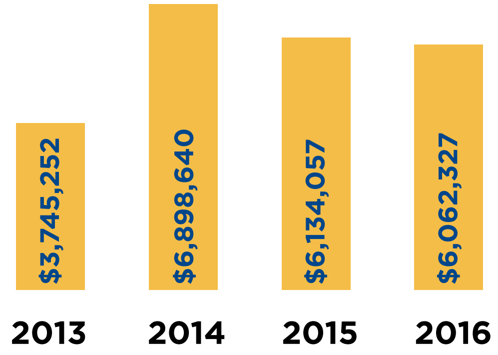
Financial Highlights

2013-2016

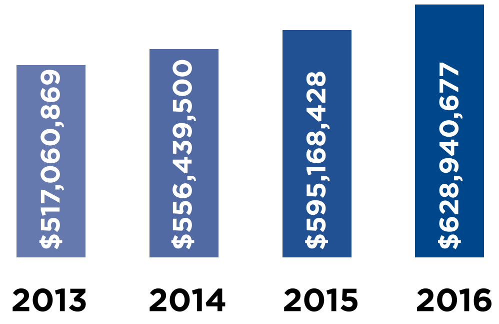
Retained Earnings



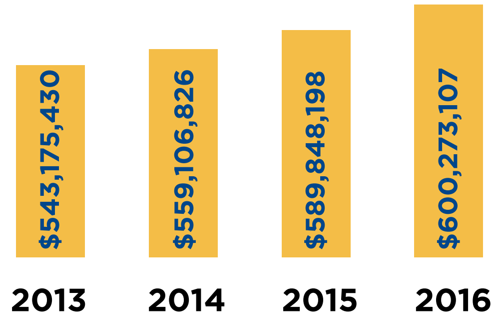
Net Income



Total Net Loans



Member Shares



Letter from the CEO

It's with great pleasure and honor that we've had the privilege of serving you, our member-owners for over 81 years. During the Great Depression of the 1930s, credit unions started to be "noticed" nationally. In 1936 the Federal Credit Union Act was created and at that time, legitimate financial institutions for people of lesser means (with a 40% unemployment rate then, MANY people were of "lesser means") were sorely needed. As such, credit unions came into being as an alternative to banks. In those days, many credit unions were literally operating out of a shoebox or a cigar box, and of course via all manual ledgers. Many operated only part-time.

Fortunately for consumers, credit unions (and not only in the USA) have survived nicely over the last 8 decades, adopting new technologies to compete effectively, and have succeeded in building up their financial reserves to be able to weather the periodic hard economic times, such as the Great Recession of 2007-2008 when the real estate value growth bubbles burst. Our Credit Union, as you should know, is one of the strongest and most stable in the country, with a net worth to assets ratio of 14%. A little over 30 years ago, that ratio was a too-low 4%. You can see our reserves position, which has grown over $100 million in that time period, on our balance sheet included in this Annual Report. Just as Farmers has been focused on remaining highly competitive and stable, so has your Credit Union. Both have succeeded in these most basic of quests.

We continue to invest in new technology and in our employees, the latter being our number one off-balance sheet asset (And that is not mere CEO rhetoric; it is real.) and the former being our number two asset. Our continuing number one strategic goal is to make it progressively easier for you to do business with us. We touch your lives literally every day, in being your savings, checking, and borrowing guardian/provider. Occasionally, tracking money can get complicated and a little difficult even to understand. We are here to help you solve your money challenges and goals. We come to work every day to solve and prevent the problems that can arise in the normal course of business, and to create a strong future for you and the Credit Union, by improving our members' financial lives.

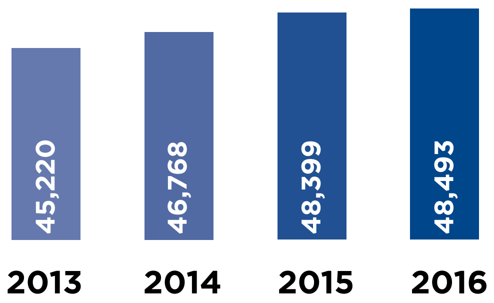
Again this year, we are proud to present you with a "clean," unqualified CPA opinion report on the pages that follow. Should you have any questions, please feel free to contact me at mherter@figfcu.org, or call our toll-free number, ext. 6001. Thank you for choosing to do business with your Credit Union family.

Mark Herter, Chief Executive Officer

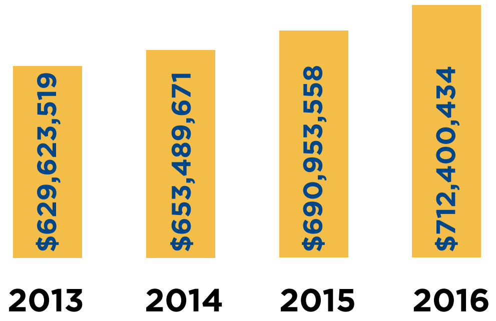
Credit Union Highlights

2013-2016

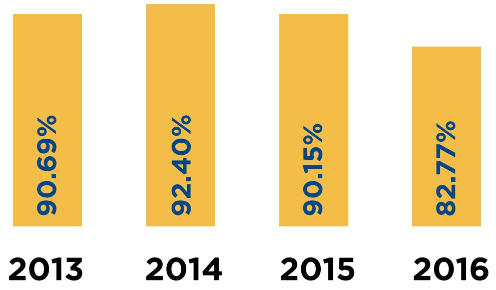
Total Members



Total Assets



Member Satisfaction



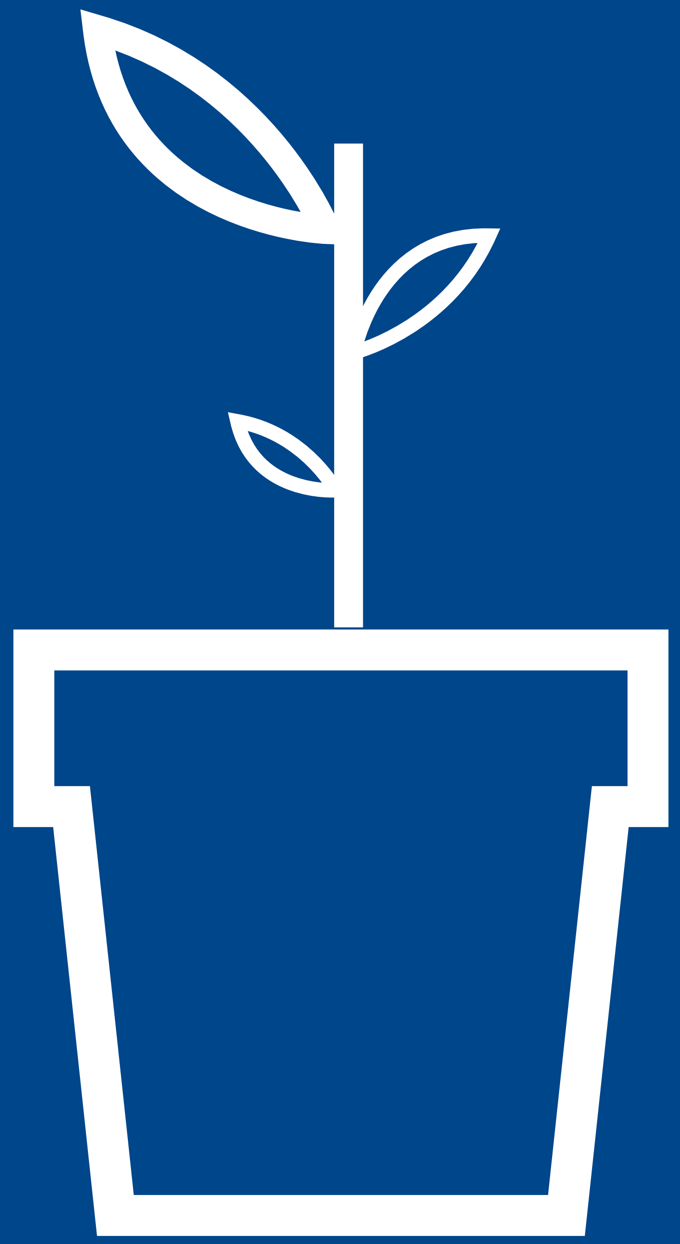
Board of Directors

Top Row (L–R): **Rudy Trevino** Chief Compliance Officer, FGI, **Michael Ashe** Agent, **Scott Lindquist** Chairman of the Board, Executive Vice President and Chief Financial Officer, **Jim Snikeris** Retired **Ed McMahan** District Manager, **Lewis Williams** Chairman, SFUZ, Director of IT Finance

Bottom Row (L– R): **Frank Ceglar** Retired, **Marilyn Huntamer** Agent, **Linda Sanazaro** Head of Enterprise Operations, **Paul Crosetti** Director, Head of Sales and Agency Management. Not in Picture: **Danny Davison** District Manager

Management Team

Left to Right: **Mark Herter** CEO, **Laura Campbell** President, **Brian Leonard** Chief Lending Officer, **Kathy Chicas** Chief Operations Officer, **Harland Bengs** Chief Financial Officer, **Beth Rodgers** Chief Marketing Officer, **Yusef Mustafa** Chief Technology Officer



1936

Farmers Insurance Group Federal Credit Union opens for business. Our offices are located at 4680 Wilshire Boulevard, just down the street from our current Home Office.

The Late 1920s/ Early 1930s

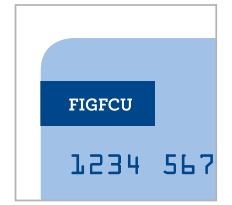
In the late 1920s, Farmers Insurance opens its first office in Los Angeles and offers credit services to its customers. This is the early seed from which a credit union will emerge in 1936, just two years after credit unions were formally ratified by federal law.

The 1950s

In 1956 the first branches open in Simi Valley, Merced and Colorado Springs. The largest branch carries a mere $500 cash on hand. A year later the Credit Union appoints a Board of Directors, and the number of branches doubles.

The 1980s

In 1984 the Credit Union gets its first software system to run operations. By 1987, membership has reached 23,000 and assets top $78 million. The following year the first branch is automated, replacing manual entries and daily faxes to Home Office.



Credit Card Intro
(early 80s)

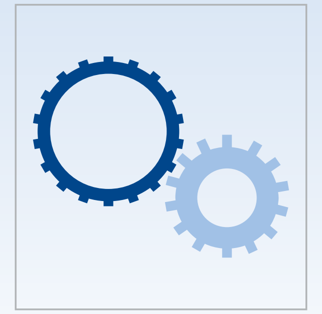
First ATM
(late 80s)

Fonline
(late 80s)

2016

Rebranding

The Credit Union rebrands to celebrate our family values and remind us daily of our commitment to members: service and performance. Our brand "identity" signifies our commitment to growth, stability and reliability. Just like us!



Core Conversion

This complex systems upgrade, which tests the resiliency of staff and members alike, greatly improves our capability to serve members with excellence, and introduce new products and services more quickly and effectively.

The 1990s

In 1991 Credit Union assets total $120 million, and reserves $12 million. Five years later Online Banking makes its debut, and in 1999 Home Loans are added to the growing list of products and services.

Debit Card Intro
(Mid 90s)

The 2000s

In 2005 we introduce Commercial Real Estate loans to provide agents with a means to finance their office buildings and continue to grow their agencies.

2010 & Beyond

This busy period sees the 2011 introduction of Student Loans and membership topping 43,000. Assets now exceed 500 million, a fourfold increase over the prior 20 years.

In 2012 the CU Gives Back program is launched to return excess profit to members in the form of cash bonuses.

DoerenMayhew
CPAs AND ADVISORS

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Independent Auditor's Report

March 31, 2017

To the Supervisory Committee and Board of Directors
of Farmers Insurance Group Federal Credit Union

Report on the Financial Statements

We have audited the accompanying financial statements of Farmers Insurance Group Federal Credit Union, which comprise the statements of financial condition as of December 31, 2016 and 2015, and the related statements of income, comprehensive income, members' equity and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these 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 financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these 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 audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the 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 entity'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 financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Insight. Oversight. Foresight.®

Known Internationally as Moore Stephens Doeren Mayhew, P.C. An Independent Firm Associated With Moore Stephens International Limited.

To the Supervisory Committee and Board of Directors
of Farmers Insurance Group Federal Credit Union

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Farmers Insurance Group Federal Credit Union, as of December 31, 2016 and 2015, 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.

Doeren Mayhew

Doeren Mayhew
Miami, FL

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF FINANCIAL CONDITION
AS OF DECEMBER 31, 2016 AND 2015

Assets	2016	2015
Cash and cash equivalents	$27,435,126	$30,153,485
Interest bearing deposits	10,926,000	18,585,000
Investments:		
Available-for-sale	9,564,076	12,763,786
Held-to-maturity	8,590,000	9,874,550
Loans to members, net of allowance for loan losses	628,940,677	595,168,428
Accrued interest receivable	2,768,542	2,428,931
Federal Home Loan Bank stock	1,686,600	1,646,200
Prepaid and other assets	12,796,577	12,634,102
Property and equipment	3,812,704	2,145,141
NCUSIF deposit	5,880,132	5,553,935
Total assets	$712,400,434	$690,953,558
Liabilities and Members' Equity		
Liabilities:		
Members' shares and savings accounts	$600,273,107	$589,848,198
Borrowings	5,537,894	—
Accrued expenses and other liabilities	6,584,278	7,154,181
Total liabilities	612,395,279	597,002,379
Commitments and contingent liabilities		
Members' equity:		
Regular reserve	16,966,743	16,966,743
Undivided earnings	82,992,027	76,929,700
Accumulated other comprehensive income	46,385	54,736
Total member's equity	100,005,155	93,951,179
Total liabilities and members' equity	$712,400,434	$690,953,558

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF INCOME
YEARS ENDED DECEMBER 31, 2016 AND 2015

	2016	2015
Interest income:		
Loans to members	$35,883,003	$33,630,996
Investment securities	834,995	538,724
Total interest income	36,717,998	34,169,720
Interest expense:		
Members' shares and savings accounts	3,513,898	3,194,674
Borrowings	31,134	—
Total interest expense	3,545,032	3,194,674
Net interest income	33,172,966	30,975,046
Provision for loan losses	3,107,718	1,473,333
Net interest income after provision for loan losses	30,065,248	29,501,713
Non-interest income:		
Overdraft and share draft fees	3,362,978	3,412,417
Service charges and other fees	2,683,852	2,716,832
Refund from pension plan	1,745,703	—
Interchange income	1,208,592	1,327,788
Other income	706,228	612,382
Total non-interest income	9,707,353	8,069,419
Non-interest expenses:		
Compensation and benefits	17,891,799	17,043,509
Office operating costs	7,630,882	6,268,016
Educational and promotional expense	2,555,128	2,606,057
Office occupancy	1,578,712	1,596,837
Other expenses	1,406,910	1,469,837
Loan servicing expense	1,326,243	1,331,936
Professional and outside services	1,320,600	1,120,883
Total non-interest expenses	33,710,274	31,437,075
Net income	$6,062,327	$6,134,057

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF COMPREHENSIVE INCOME
YEARS ENDED DECEMBER 31, 2016 AND 2015

	2016	2015
Net income	$6,062,327	$6,134,057
Other comprehensive income/(loss):		
Available-for-sale investments:		
Net unrealized holding losses on available-for-sale investments	(8,351)	(81,861)
Reclassification adjustment for investment (gains)/losses included in net income	—	—
Total other comprehensive loss	(8,351)	(81,861)
Comprehensive income	$6,053,976	$6,052,196

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF MEMBERS' EQUITY
YEARS ENDED DECEMBER 31, 2016 AND 2015

	Regular Reserve	Undivided Earnings	Accumulated Other Comprehensive Income	Total
Balance, December 31, 2014	$16,966,743	$70,795,643	$136,597	$87,898,983
Net income	—	6,134,057	—	6,134,057
Other comprehensive loss	—	—	(81,861)	(81,861)
Balance, December 31, 2015	16,966,743	76,929,700	54,736	93,951,179
Net income	—	6,062,327	—	6,062,327
Other comprehensive loss	—	—	(8,351)	(8,351)
Balance, December 31, 2016	$16,966,743	$82,992,027	$46,385	$100,005,155

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2016 AND 2015

	2016	2015
Cash flows from operating activities:		
Net income	$6,062,327	$6,134,057
Adjustments to net cash provided from operating activities:		
Provision for loan losses	3,107,718	1,473,333
Depreciation and amortization	1,205,911	805,099
Amortization of investment premiums/discounts, net	550	29,233
Changes in assets and liabilities:		
Net change in accrued interest receivable	(339,611)	(130,839)
Net change in prepaid and other assets	(162,475)	(1,181,442)
Net change in accrued expenses and other liabilities	(569,903)	670,319
Net cash provided from operating activities	9,304,517	7,799,760

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2016 AND 2015

Cash Flows (Continued)

	2016	2015
Cash flows from investing activities:		
Interest bearing deposits	7,659,000	(5,699,000)
Proceeds from maturities and repayments of available-for-sale investments	3,191,359	3,571,122
Proceeds from the maturity of held-to-maturity investments	1,524,000	6,292,000
Purchase of held-to-maturity investments	(240,000)	(5,240,000)
Purchase of FHLB stock	(40,400)	(1,646,200)
Net change in loans to members, net of charge-offs	(36,879,967)	(40,202,261)
Expenditures for property and equipment	(2,873,474)	(1,433,993)
Net change in NCUSIF deposit	(326,197)	(165,367)
Net cash used in investing activities	(27,985,679)	(44,523,699)
Cash flows from financing activities:		
Net change in members' shares and savings accounts	10,424,909	30,741,372
Proceeds from borrowings	5,537,894	—
Net cash provided from financing activities	15,962,803	30,741,372
Net change in cash and cash equivalents	(2,718,359)	(5,982,567)
Cash and cash equivalents - beginning	30,153,485	36,136,052
Cash and cash equivalents - ending	$27,435,126	$30,153,485

Supplemental Information

	2016	2015
Interest paid	$3,545,032	$3,194,674

See accompanying notes to the financial statements.

Note 1 - Nature of Business and Significant Accounting Policies

Organization

Farmers Insurance Group Federal Credit Union (the Credit Union) is a cooperative association organized in accordance with the provisions of the Federal Credit Union Act for the purpose of promoting thrift among, and creating a source of credit for, its members. Participation in the Credit Union is limited to those individuals who qualify for membership. The field of membership is defined by the Credit Union's Charter and Bylaws.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the dates of the financial statements and the reported amounts of revenues and expenses for the periods then ended. Actual results could differ from those estimates. Estimates that are particularly susceptible to change include the determination of the allowance for loan losses. The significant accounting principles and policies used in the preparation of these financial statements, together with certain related information, are summarized below.

Concentrations of Credit Risk

A significant amount of the Credit Union's business activity is with members who are employees or former employees of Farmers Insurance Group Inc. The Credit Union also may be exposed to credit risk from a regional economic standpoint, since a significant concentration of its borrowers work or reside in the state of California. However, the loan portfolio is well diversified and the Credit Union does not have any significant concentration of credit risk, except unsecured loans, which by their nature, increase the risk of loss compared to those loans that are collateralized.

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Comprehensive Income/(Loss)

Accounting principles generally require the recognized revenue, expenses, gains and losses be included in net income. Certain changes in assets and liabilities are reported in a separate component of comprehensive income/(loss). Other comprehensive income/(loss) is limited to the changes in unrealized gain/(loss) on available-for-sale investments. When available-for-sale investments are sold, the gain or loss realized on the sale is reclassified from accumulated other comprehensive income/(loss) to the gain or loss on sale of investments reported on the statements of income.

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents includes cash on hand, amounts due from banks and corporate credit unions (including cash items in the process of clearing) and interest-bearing deposits in banks and corporate credit unions with an original maturity of 90 days or less including overnight deposits. Amounts due from banks and corporate credit unions may, at times, exceed federally insured limits.

Interest Bearing Deposits

Interest bearing deposits are time deposits with financial institutions with an original maturity in excess of 90 days. These deposits are all 100% insured as no deposit to one individual institution exceeds $250,000.

Investments

Investments are classified into the following categories: held-to-maturity and available-for-sale. Investments classified as held-to-maturity are measured at amortized cost. This classification is based upon the Credit Union's intent and ability to hold these investments to full maturity. Investment classified as available-for-sale are measured at fair value as of the statement of financial condition date. Unrealized gains and losses on available-for-sale investments are reported as a separate component of members' equity. Realized gains and losses on disposition, if any, are computed using the specific identification method. Investments are adjusted for the amortization of premiums and accretion of discounts as an adjustment to interest income on investments over the term of the investment by a method which approximates the interest method.

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Investments (Continued)

Declines in the estimated fair value of individual investments below their cost that are other-than-temporary are reflected as realized losses in the statements of income. Factors affecting the determination of whether an other-than-temporary impairment has occurred include, among other things, (i) the length of time and the extent to which the fair value has been less than cost, (ii) the financial condition and near term prospects of the issuer, (iii) that the Credit Union does not intend to sell these investments, and (iv) it is more likely than not that the Credit Union will not be required to sell before a period of time sufficient to allow for any anticipated recovery in fair value.

Federal Home Loan Bank (FHLB) Stock

As a member of the FHLB, the Credit Union is required to invest in stock of the FHLB. The FHLB stock is carried at cost and its disposition is restricted. Based on its restricted nature, no ready market exists for this investment and it has no quoted market value.

Loans to Members

Loans that the Credit Union has the intent and ability to hold for the foreseeable future are stated at unpaid principal balances, less an allowance for loan losses and net deferred loan origination fees and costs. Interest on loans to members is recognized over the terms of the loans and is calculated on principal amounts outstanding.

The accrual of interest on loans is discontinued at the time the loan is 90 days delinquent unless the credit is well-secured and in the process of collection. Past due status is based on contractual terms of the loan. In all cases, loans are placed on non-accrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not collected for loans that are placed on non-accrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Loans to Members (Continued)

Loan fees and direct loan origination costs are deferred and the net fee or cost is recognized as an adjustment to interest income on loans using a method that approximates the interest method over the estimated life of the loans.

Allowance for Loan Losses

The allowance for loan losses (“allowance”) is an estimate of loan losses inherent in the Credit Union’s loan portfolio. The allowance is established through a provision for loan losses which is charged to expense. Loan losses are charged off against the allowance when the Credit Union determines the loan balance to be uncollectible. Cash received on previously charged-off amounts is recorded as a recovery to the allowance.

The allowance is evaluated on a regular basis by management and is based upon management’s periodic assessment of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower’s ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

For the purpose of determining the allowance disclosures, the Credit Union has segmented loans in the portfolio by product type. Loans are divided into the following segments: Consumer, Residential Real Estate, and Commercial. The Credit Union further disaggregates these segments into classes based on the associated risks within those segments. Consumer loans are divided into three classes: Unsecured, Automobile, and Other secured. Residential real estate loans are divided into three classes: First mortgage, Second mortgage, and Home equity line of credit (HELOC). Commercial loans are divided into three classes: Agency secured, Agency unsecured and Real estate. Each class of loans requires significant judgment to determine the estimation method that fits the credit risk characteristics of its portfolio segment. The Credit Union uses both internally developed and vendor supplied models in the process. The vendor model is supplied by P360, Inc. The P360, Inc. model provides meaningful insights into the portfolio’s risk composition, as dictated by the intrinsic value and other relevant market data. The model is specifically designed to calculate the risk of the loan portfolio on an individual loan level basis to provide optimal loss coverage analysis over the next 12 months.

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Allowance for Loan Losses (Continued)

The allowance consists of specific and general components. The specific component covers impaired loans and troubled debt restructurings and the specific allowances are established for these loans based on a thorough analysis of the most probable source of repayment, including the present value of the loan's expected future cash flows, the loan's estimated market value, or the estimated fair value of the underlying collateral. The general component covers non-impaired loans and is based on historical losses adjusted for current factors. This actual loss experience is adjusted for economic factors based on the risks present for each portfolio segment or class of loans. These economic factors include consideration of the following: levels of and trends in delinquencies and impaired loans; levels of and trends in charge-offs and recoveries; trends in volume and terms of loans; effects of any changes in risk selection and underwriting standards; other changes in lending policies, procedures, and practices; experience, ability, and depth of lending management and other relevant staff; national and local economic trends and conditions; industry conditions; and effects of changes in credit concentrations. These factors are inherently subjective and are driven by the repayment risk associated with each portfolio segment. The Credit Union maintains a separate general valuation allowance for each portfolio segment.

Consumer Segment Allowance Methodology

For consumer loans, the Credit Union determines the allowance on a collective basis utilizing historical and forecasted losses to represent the best estimate of inherent losses at the measurement date. Loans are pooled, generally by loan types with similar risk characteristics. The Credit Union identifies consumer loans that underwent a troubled debt restructuring and evaluates these loans on an individual basis. In addition, the allowance model incorporates numerous other historical factors based upon the borrower, collateral type, loan performance, environment, and economy. These historical factors used in the analysis date back to 2001.

As appropriate, to achieve greater accuracy, further stratification of a selected portfolio may occur such as by year of origination, geographic location and other predictive characteristics. The consumer allowance model primarily uses historical delinquency and default experience. Information on forecasted delinquency analysis, member credit score trends, unemployment trends, industry trends and other key economic variables that may influence the frequency and severity of losses for each class of loan within the consumer segment may also be considered. Loans collateralized by a certificate or share account are considered fully secured unless otherwise notified.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Allowance for Loan Losses (Continued)

Residential Real Estate Segment Allowance Methodology

For residential real estate loans not identified as impaired, the Credit Union determines the allowance on a collective basis, utilizing various economic and financial simulations in order to determine the best estimate of inherent losses at the measurement date. Loans are pooled, generally by loan types with similar risk characteristics. In addition, the allowance model incorporates numerous other historical factors based upon the borrower, collateral type, loan performance, environment, and economy. These historical factors used in the analysis date back to 2001.

As appropriate, to achieve greater accuracy, further stratification of a selected portfolio may occur such as by year of origination, geographic location and other predictive characteristics. Information on member credit score trends, combined loan to value ratios, home price trends, unemployment trends, industry trends, and other key economic variables that may influence the frequency and severity of losses for each class of loan within the residential real estate segment may also be considered. The residential real estate allowance also includes an amount for the estimated losses on individually evaluated impaired loans.

Additionally, a mortgage sample analysis is performed periodically to assess the potential loss exposure within the residential real estate loan portfolio. The Credit Union obtains updated property values on all existing real estate loans in its portfolio. Using a sample of loans, the Credit Union performs individual reviews to assess the potential loss exposure based on various risk factors including combined loan to value, member credit score, delinquency, loan vintage, and type of collateral. Results of the sample analysis are extrapolated to the total population to assess the adequacy of the allowance.

Commercial Segment Allowance Methodology

For commercial loans not identified as impaired, the Credit Union determines the allowance on a collective basis utilizing historical and forecasted losses to represent the best estimate of inherent losses at the measurement date. In addition, the allowance model incorporates numerous other historical factors based upon the borrower, collateral type, loan performance, environment, and economy. These historical factors used in the analysis date back to 2001.

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Allowance for Loan Losses (Continued)

Commercial Segment Allowance Methodology (Continued)

Loss estimates for the commercial loan portfolio segment may be adjusted as appropriate based on credit risk assessment and management's analysis of leading predictors of losses, as well as additional analysis of long-term average loss experience compared to previously forecasted losses, external loss data, or other risks identified from current economic conditions and credit quality trends. The commercial allowance may also include an additional allowance for individually evaluated high risk loans and an amount for the estimated losses on individually evaluated impaired loans.

The Credit Union's commercial loan portfolio also includes loans collateralized by contract value. These are considered fully secured unless notified otherwise, as these loans, when written within the guidelines established by Farmers, are secured and will be paid in full by Farmers upon member termination if the Credit Union's collection efforts were to ultimately fail.

Impaired Loans

A loan is considered impaired when, based on current information and events, it is probable that the Credit Union will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral, less costs to sell, if the loan is collateral dependent. A loan is collateral dependent if its repayment is expected to be provided solely by the underlying collateral.

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Troubled Debt Restructurings

Under certain circumstances, the Credit Union will provide borrowers relief through loan restructurings. A loan restructuring represents a troubled debt restructuring ("TDR") if for economic or legal reasons related to the borrower's financial difficulties the Credit Union grants a concession to the borrower that it would not otherwise consider. Restructured loans typically present an elevated level of credit risk as the borrowers are not able to perform according to the original contractual terms. Loans that are reported as TDRs are considered impaired and measured for impairment as described above.

Credit Quality Indicators

The Credit Union uses the P360, Inc. model to monitor credit quality for the consumer, residential real estate, and commercial loan portfolios. The P360, Inc. model analyzes each loan's risk. When analyzing each loan, the model identifies a set of numbers, or vectors, which represent the borrower's probability of default and the loss severity of the loan over a set of different economic scenarios. These vectors are used to calculate the loan risk grade and run risk adjusted cash flows which result in the value-at-risk, pricing, and loan valuation.

The model incorporates over 150 data points covering more than credit score and collateral value. These loan level factors include institution and borrower specific data points as well as economic measures that feed into the risk analysis. They provide value reconciliation when refreshing property values and add updated values for the new and used auto portfolios. They continue to enhance the risk model by incorporating new technologies and applying all loan data available. In addition to credit score, the model incorporates numerous other factors based upon the borrower, collateral, loan performance, environment, institution, and economy as follows:

Macro-economic - This segment's data points are used to depict the overall health of the national economy such as: national unemployment, GDP growth, Treasury rate curves and forecasts, industry delinquencies and charge-offs, national credit scores, borrower bankruptcy rates, etc.

Institution - This segment focuses on the Credit Union and is used to model the borrower's profile, stability, and fine tune the risk adjustments to the specific institution. Examples of data points include delinquency rates and trends, charge-offs, and bankruptcies per 1,000 members.

Regional geography - This segment focuses on local economic factors such as unemployment, growth, and real estate values.

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Credit Quality Indicators (Continued)

Loan - Additional data points added to this analysis are payment trend, auto pay, updated senior balances, last payment amounts, and use of proceeds.

Borrower - Examples of data points in this segment are disposable income, updated cash reserves, employment status, and direct deposit.

Asset - In addition to using different automated valuation model products for the residential portfolio, the model includes new data to improve vehicle valuations for the new and used auto portfolios.

The model assigns a risk grade to all loans. Category ratings are reviewed quarterly, at which time management analyzes the resulting grades, as well as other external statistics and factors, to track loan performance. The risk ratings from Extensia Financial, LLC are taken into consideration when the P360, Inc. risk grades are applied to the individual commercial real estate loan participations.

The P360, Inc. risk grades are as follows:

V1 - Minimal risk - These loans generally show the ability to cover expenses with a minimal chance of default. The typical characteristics for these loans are long-term Credit Union members with excellent credit history, strong cash flow, quality money management, excellent access to alternative sources of financing, and well collateralized. These loans typically have very low potential loss, no greater than one percent of the loan balance in most cases when factoring the default probability and loss severity.

V2 - Low risk - These loans generally reflect good payment history, a healthy loan to value ratio and are adequately collateralized. The borrowing entity has very good to excellent credit, steady cash flow, quality money management, and good access to alternative sources of financing. As a result, the risk category is highly unlikely to experience a loss. If a loss does occur, it is likely to be minimal.

V3 - Acceptable risk - These loans are better than average loans with a low chance of a loss. The potential loss should be no greater than five percent of the loan balance when factoring default probability and loss severity. Most of the risk attributes for these loans are in line with a low risk profile but are on the fringe of adding risk. Borrower has some access to alternative sources of financing, good money management, and shows control of expenses.

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Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Credit Quality Indicators (Continued)

V4 - Moderate risk - These loans have potential weaknesses or may show a propensity to deteriorate further. These loans are the start of the tipping point of the mid-range risk grades (V4 - V6) that tend to move either to a worsening position or a healthier position and is measured by a ten percent value at risk. This risk grade may include borrowers with only medium to fair credit ratings and a few recent problems. Cash flow is steady and generally adequate to service debt but may be subject to cyclical conditions. The borrower may have limited access to alternative financing.

V5 - Special mention - These loans can prove to be in the most critical stage. Most loans tend to either move up or down from the mid-range risk grades (V4 - V6). Both credit and collateral are substandard, with external economic factors bearing down. The outstanding loan balance may not be entirely protected by equity in the underlying asset with up to a fifteen percent potential loss produced by probability and severity. There may be one or more specific weaknesses jeopardizing the loan, and the Credit Union will most likely sustain a loss if the deficiencies are not corrected.

V6 - Increased risk - These loans generally have multiple vulnerable and weak risk factors that could be attributed to local economic factors. On the basis of currently known facts, the combination of weak attributes make collection or liquidation in full highly questionable and improbable. The risk grade is defined by potential losses of up to twenty percent of the loan balance.

V7 - Elevated risk - There is a strong probability that the Credit Union may not be able to recover on these loans. The Credit Union and the member must look at all options, including modification. Liquidation needs to be considered because most of the underlying assets for this risk grade have passed the tipping point. A loss is nearly impossible to avoid on repayment, refinancing, or liquidation for these loans. The value at risk could be upwards of thirty percent of the current loan balance.

V8 - Doubtful - These borrowers are most likely in a loss situation and can be measured by potential value at risk between thirty and forty percent of the outstanding loan balance. In most cases, assets in this region do not recover and the members and properties are being worked with directly. The most current information on the member and asset has been acquired and the Credit Union has a firm estimate of the loss when the time arrives.

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Credit Quality Indicators (Continued)

V9 - Inherent loss - These loans are considered uncollectible and will be charged off immediately. Assets in this risk area have an inherent value at risk, north of forty percent. Modification is impossible without major concessions or write down. Residential and commercial properties have a high probability of becoming other real estate owned. In some cases, the Credit Union may find a glimmer of success in short sale opportunities. Other real estate owned, having extended liquidation times and expenses are most likely in less than optimal locations. Conditions prove challenging to draw respectable tenants and rent.

Loan Charge-off Policies

The Credit Union's quality control process includes preparing lists to monitor and track delinquent loans. Tracking the loans on these lists enables management to assess the performance of the loan portfolio and act to mitigate risk therein through necessary changes in policy and procedures. The quality control process also serves as a tool to assist the Credit Union in identifying loans for charge-off on a timely basis.

Consumer, residential real estate, and commercial loans are generally charged-off when the loan is deemed to be uncollectible. A loan is deemed uncollectible when:

- the member has gained relief through bankruptcy;
- the loan is a deficiency balance from the sale of collateral and the borrower has indicated an unwillingness to make further payments;
- the borrower is determined to be a "skip";
- the member is deceased, collateral has been liquidated and there is no co-maker or estate to pursue for payment;
- the loan is 180 days or more delinquent, unless one of the following conditions exists:
    - the borrower is making monthly payments but cannot qualify for refinancing or re-aging;
    - the Credit Union or the member is waiting for settlement of a documented insurance/bond claim;
    - the borrower is deceased, and the Credit Union has substantial reason to expect settlement from the estate, co-makers, or relatives;
    - the Credit Union is waiting for the proceeds from the sale of repossessed collateral.

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NOTES TO THE FINANCIAL STATEMENTS
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Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Loan Charge-off Policies (Continued)

Uncollectible loans to be charged off to the allowance are approved by the Board of Director each month. For repossessed collateral, including foreclosed property, the loan is charged off to the allowance and the net realizable value moved to other assets.

Property and Equipment

Property and equipment are carried at cost, less accumulated depreciation and amortization. Depreciation is computed principally by the straight-line method based upon the useful lives of the related assets. The cost of leasehold improvements is amortized using the straight-line method over the term of the lease, or the estimated life of the asset, whichever is less. The Credit Union reviews property and equipment (long-lived assets) for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Maintenance, repairs, and minor alterations are charged to current operations as expenditures occur and major improvements are capitalized.

NCUSIF Deposit

The deposit in the National Credit Union Share Insurance Fund (NCUSIF) is in accordance with NCUA regulations, which require the maintenance of a deposit by each insured credit union in an amount equal to one percent of its insured shares. The deposit would be refunded to the Credit Union if its insurance coverage is terminated, it converts to insurance coverage from another source, or the operations of the fund are transferred from the NCUA Board. The NCUSIF deposit is required to be periodically reviewed for impairment.

Perpetual Contributed Capital

As a requirement of membership, the Credit Union maintains a Perpetual Contributed Capital (PCC) account with Catalyst Corporate Federal Credit Union (CCFCU) of $600,000. The PCC is not subject to share insurance coverage by the NCUSIF or other deposit insurer. The PCC is not releasable due solely to a merger, charter conversion or liquidation and is callable at the option of CCFCU. The PCC has a perpetual maturity and a noncumulative dividend. The PCC is included with prepaid and other assets in the statements of financial condition.

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Members' Shares and Savings Accounts

Members' shares are the savings deposit accounts of the owners of the Credit Union. Share ownership entitles the members to vote in annual elections of the Board of Directors. Irrespective of the amount of shares owned, no member has more than one vote.

Members' shares are subordinated to all other liabilities of the Credit Union upon liquidation. Interest on members' shares and savings accounts is based on available earnings at the end of an interest period and is not guaranteed by the Credit Union. Interest rates on members' share accounts are set by the Board of Directors, based on an evaluation of current and future market conditions.

Borrowings

The Credit Union has outstanding borrowings from the FHLB of San Francisco. FHLB borrowings are secured by qualified collateral, as defined in the FHLB Statement of Credit Policy.

Regular Reserve

The Credit Union is required to maintain a statutory reserve (regular reserve) in accordance with the Federal Credit Union Act. This statutory reserve represents a regulatory restriction and is not available for the payment of interest.

Income Taxes

The Credit Union is exempt from most federal, state, and local taxes under the provisions of the Internal Revenue Code and state tax laws. The Income Taxes Topic of the FASB ASC clarifies accounting for uncertainty in income taxes reported in the financial statements. The interpretation provides criteria for assessment of individual tax positions and a process for recognition and measurement of uncertain tax positions. Tax positions are evaluated on whether they meet the "more likely than not" standard for sustainability on examination by tax authorities. Federal credit unions are tax-exempt under Internal Revenue Code sections 501(c)(1)(a)(I) and 501(c)(14)(A). As such, the Credit Union has no uncertain tax positions that qualify for either recognition or disclosure in the financial statements. Additionally, no interest or penalties have been recorded in the accompanying financial statements related to uncertain tax positions.

Reclassification

Certain amounts reported in the 2015 financial statements have been reclassified to conform to the 2016 presentation.

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Recent Accounting Pronouncements

On January 5, 2016, the FASB issued Accounting Standards Update 2016-01, Financial Instruments - Overall: Recognition and Measurement of Financial Assets and Financial Liabilities (the ASU). The changes to the current GAAP model primarily affect the accounting for equity investments, financial liabilities under the fair value option, and the presentation and disclosure requirements for financial instruments. The accounting for other financial instruments, such as loans, investments in debt securities, and financial liabilities is largely unchanged. The classification and measurement guidance will be effective for non-public business entities in fiscal years beginning after December 15, 2018, or they may early adopt for periods after December 15, 2017. The Credit Union is currently evaluating the impact of the ASU.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments-Credit Losses. The ASU introduces a new accounting model, the Current Expected Credit Losses model (CECL), which requires earlier recognition of credit losses. The FASB's CECL model utilizes a lifetime "expected credit loss" measurement objective for the recognition of credit losses for loans, held-to-maturity securities and other receivables at the time the financial asset is originated or acquired. The expected credit losses are adjusted each period for changes in expected lifetime credit losses. For available-for-sale securities where fair value is less than cost, credit-related impairment, if any, will be recognized in an allowance for credit losses and adjusted each period for changes in expected credit risk. This model replaces the multiple existing impairment models in current GAAP, which generally require that a loss be incurred before it is recognized. The ASU will be effective for credit unions on December 31, 2021. Early application is permitted for annual periods beginning January 1, 2019.

In February 2016, the FASB issued ASU No. 2016-02, Leases, which is intended to increase transparency and comparability of accounting for lease transactions. The ASU will require lessees to recognize most leases on the balance sheet as lease assets and lease liabilities and will require both quantitative and qualitative disclosures regarding key information about leasing arrangements. Lessor accounting is largely unchanged. The guidance is effective December 31, 2020 with an option to early adopt. The Credit Union is evaluating whether to early adopt and the effect that ASU 2016-02 will have on its financial statements, regulatory capital and related disclosures.

Subsequent Events

Management has evaluated subsequent events through March 31, 2017, the date the financial statements were available to be issued. Management has not identified any items requiring recognition or disclosure.

Note 2 - Investments

The following tables present the amortized cost and estimated fair value of investments as of December 31, 2016:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
Mortgage-backed securities	$1,346,811	$50,398	$—	$1,397,209
NCUA guaranteed notes	8,152,509	1,734	(5,792)	8,148,451
Collateralized mortgage obligations	18,371	45	—	18,416
	$9,517,691	$52,177	($5,792)	$9,564,076

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Held-to-maturity:				
Negotiable certificates of deposit	$8,590,000	$13,273	($669)	$8,602,604

The following tables present the amortized cost and estimated fair value of investments as of December 31, 2015:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
Mortgage-backed securities	$1,656,757	$55,063	$—	$1,711,820
NCUA guaranteed notes	11,028,402	19,307	(19,694)	11,028,015
Collateralized mortgage obligations	23,891	60	—	23,951
	$12,709,050	$74,430	($19,694)	$12,763,786

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Note 2 - Investments (Continued)

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Held-to-maturity:				
Negotiable certificates of deposit	$9,874,550	$2,143	($38,799)	$9,837,894

The amortized cost and estimated fair value of debt securities as of December 31, 2016, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available-for-sale		*Held-to-maturity*	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Within one year	$—	$—	$5,470,000	$5,478,104
1 to 5 years	—	—	3,120,000	3,124,500
Mortgage-backed securities	1,346,811	1,397,209	—	—
NCUA guaranteed notes	8,152,509	8,148,451	—	—
Collateralized mortgage obligations	18,371	18,416	—	—
Total	$9,517,691	$9,564,076	$8,590,000	$8,602,604

Information pertaining to investments with gross unrealized losses as of December 31, 2016, aggregated by investment category and length of time that individual investments have been in a continuous loss position, follows:

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Available-for-sale:						
NCUA guaranteed notes	$2,869,844	($5,792)	$—	$—	$2,869,844	($5,792)

Note 2 - Investments (Continued)

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Held-to-maturity:						
Negotiable certificates of deposit	$99,847	($153)	$99,485	($516)	$199,332	($669)

Information pertaining to investments with gross unrealized losses as of December 31, 2015, aggregated by investment category and length of time that individual investments have been in a continuous loss position, follows:

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Available-for-sale:						
NCUA guaranteed notes	$3,492,183	($19,694)	$—	$—	$3,492,183	($19,694)

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Held-to-maturity:						
Negotiable certificates of deposit	$5,846,221	($32,865)	$2,524,066	($5,934)	$8,370,287	($38,799)

Unrealized losses on securities issued by the U.S. Government and its Agencies have not been recognized into income because the implicit guarantee of the principal balances of these securities by the U.S. Government and its Agencies. The decline in fair value is primarily due to differences between security yields and market interest rates. Additionally, the decline in fair value is expected to be recovered as securities approach their maturity date and/or market rates decline. Management has the ability and intent to hold these securities through to recovery of fair value, which may be maturity. Unrealized losses on negotiable certificates of deposit have not been recognized into income because the principal balances of these deposits are guaranteed by the Federal Deposit Insurance Corporation.

Note 3 - Loans to Members

The composition of loans to members as of December 31, 2016 and 2015 is as follows:

	2016	2015
Consumer:		
Unsecured	$91,968,661	$95,550,971
Automobile	83,450,572	79,037,716
Other secured	1,791,561	1,967,417
	177,210,794	176,556,104
Residential Real Estate:		
First mortgage	92,227,528	91,442,836
Second mortgage	14,463,117	12,048,437
HELOC	25,029,915	24,934,794
	131,720,560	128,426,067
Commercial:		
Agency secured	183,342,450	174,071,575
Agency unsecured	24,033,875	16,043,679
Real estate	119,142,193	107,642,136
	326,518,518	297,757,390
Total loans	635,449,872	602,739,561
Deferred loan origination fees/costs, net	170,125	(29,880)
	635,619,997	602,709,681
Less: Allowance for loan losses	(6,679,320)	(7,541,253)
Loans to members, net	$628,940,677	$595,168,428

Note 3 - Loans to Members (Continued)

Allowance for Loan Losses

The following table presents the activity in the allowance and a summary of the allowance by portfolio segment as of and for the year ended December 31, 2016:

	Consumer	Residential Real Estate	Commercial	Total
Allowance for loan losses:				
Beginning allowance	$2,791,079	$1,584,841	$3,165,333	$7,541,253
Charge-offs	(4,217,197)	(15,806)	(363,041)	(4,596,044)
Recoveries	568,568	56,625	1,200	626,393
Provision for loan losses	4,413,558	(185,555)	(1,120,285)	3,107,718
Ending allowance	$3,556,008	$1,440,105	$1,683,207	$6,679,320
Ending balance individually evaluated for impairment	$13,589	$1,318,279	$722,142	$2,054,010
Ending balance collectively evaluated for impairment	3,542,419	121,826	961,065	4,625,310
Ending allowance	$3,556,008	$1,440,105	$1,683,207	$6,679,320

The following table presents a summary of the recorded investment in loans by portfolio segment as of December 31, 2016:

	Consumer	Residential Real Estate	Commercial	Total
Loans :				
Ending balance individually evaluated for impairment	$153,966	$8,547,298	$5,079,949	$13,781,213
Ending balance collectively evaluated for impairment	177,078,806	123,187,680	321,572,298	621,838,784
Total loans	$177,232,772	$131,734,978	$326,652,247	$635,619,997

Note 3 - Loans to Members (Continued)

Allowance for Loan Losses (Continued)

The following table presents the activity in the allowance and a summary of the allowance by portfolio segment as of and for the year ended December 31, 2015:

	Consumer	Residential Real Estate	Commercial	Total
Allowance for loan losses:				
Beginning allowance	$3,098,272	$1,919,474	$3,647,832	$8,665,578
Charge-offs	(2,628,805)	(14,850)	(285,971)	(2,929,626)
Recoveries	325,885	6,083	—	331,968
Provision for loan losses	1,995,727	(325,866)	(196,528)	1,473,333
Ending allowance	$2,791,079	$1,584,841	$3,165,333	$7,541,253
Ending balance individually evaluated for impairment	$47,735	$1,375,894	$1,957,704	$3,381,333
Ending balance collectively evaluated for impairment	2,743,344	208,947	1,207,629	4,159,920
Ending allowance	$2,791,079	$1,584,841	$3,165,333	$7,541,253

The following table presents a summary of the recorded investment in loans by portfolio segment as of December 31, 2015:

	Consumer	Residential Real Estate	Commercial	Total
Loans:				
Ending balance individually evaluated for impairment	$212,312	$7,853,068	$6,306,044	$14,371,424
Ending balance collectively evaluated for impairment	176,376,685	118,540,314	293,421,258	588,338,257
Total loans	$176,588,997	$126,393,382	$299,727,302	$602,709,681

Note 3 - Loans to Members (Continued)

Impaired Loans

The table below summarizes key information for impaired loans as of and for the year ended December 31, 2016:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With an allowance recorded:					
Consumer:					
Unsecured	$93,448	$93,448	$4,761	$122,367	$12,824
Automobile	60,518	60,522	8,828	60,773	2,370
Residential Real Estate:					
First mortgage	8,321,332	8,322,439	1,318,275	8,019,468	345,639
Second mortgage	19,469	19,469	1	63,744	4,475
HELOC	206,497	206,312	3	116,972	5,895
Commercial:					
Agency secured	22,829	22,829	838	44,067	2,503
Real estate	5,057,120	5,047,341	721,304	5,648,930	257,026
Totals by loan segment:					
Consumer	153,966	153,970	13,589	183,140	15,194
Residential Real Estate	8,547,298	8,548,220	1,318,279	8,200,184	356,009
Commercial	5,079,949	5,070,170	722,142	5,692,997	259,529
Total	$13,781,213	$13,772,360	$2,054,010	$14,076,321	$630,732

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Note 3 - Loans to Members (Continued)

Impaired Loans (Continued)

The table below summarizes key information for impaired loans as of and for the year ended December 31, 2015:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With an allowance recorded:					
Consumer:					
Unsecured	$151,285	$151,285	$26,981	$151,285	$9,280
Automobile	61,027	61,031	20,754	75,235	2,883
Residential Real Estate:					
First mortgage	7,717,603	7,725,398	1,369,884	7,717,603	310,093
Second mortgage	108,019	108,019	6,009	108,019	6,619
HELOC	27,446	27,383	1	27,446	2,259
Commercial:					
Agency secured	65,305	65,305	100	101,943	4,155
Real estate	6,240,739	6,236,653	1,957,604	6,240,739	275,675
Totals by loan segment:					
Consumer	212,312	212,316	47,735	226,520	12,163
Residential Real Estate	7,853,068	7,860,800	1,375,894	7,853,068	318,971
Commercial	6,306,044	6,301,958	1,957,704	6,342,682	279,830
Total	$14,371,424	$14,375,074	$3,381,333	$14,422,270	$610,964

Note 3 - Loans to Members (Continued)

Age Analysis of Past Due Loans

The following table presents the aging of the recorded investment in past due loans and loans on non-accrual as of December 31, 2016:

	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Current	Total loans
Consumer:						
Unsecured	$1,395,228	$505,701	$965,154	$2,866,083	$89,129,088	$91,995,171
Automobile	596,816	199,821	418,542	1,215,179	82,230,861	83,446,040
Other secured	6,301	—	—	6,301	1,785,260	1,791,561
Total	1,998,345	705,522	1,383,696	4,087,563	173,145,209	177,232,772
Residential Real Estate:						
First mortgage	843,271	1,093,463	1,297,832	3,234,566	88,984,953	92,219,519
Second mortgage	100,614	19,469	—	120,083	14,343,034	14,463,117
HELOC	330,017	206,497	—	536,514	24,515,828	25,052,342
Total	1,273,902	1,319,429	1,297,832	3,891,163	127,843,815	131,734,978
Commercial:						
Agency secured	90,821	63,273	86,427	240,521	183,101,929	183,342,450
Agency unsecured	197,408	26,695	65,270	289,373	23,744,502	24,033,875
Real estate	98,778	—	633,177	731,955	118,543,967	119,275,922
Total	387,007	89,968	784,874	1,261,849	325,390,398	326,652,247
Grand Total	$3,659,254	$2,114,919	$3,466,402	$9,240,575	$626,379,422	$635,619,997

Loans on which the accrual of interest has been discontinued or reduced approximated $3,466,000 as of December 31, 2016. There were no loans 90 days or more past due and still accruing interest as of December 31, 2016.

Note 3 - Loans to Members (Continued)

Age Analysis of Past Due Loans (Continued)

The following table presents the aging of the recorded investment in past due loans and loans on non-accrual as of December 31, 2015:

	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Current	Total Loans
Consumer:						
Unsecured	$1,113,028	$547,425	$693,999	$2,354,452	$93,234,128	$95,588,580
Automobile	568,661	231,918	239,719	1,040,298	77,992,702	79,033,000
Other secured	—	—	—	—	1,967,417	1,967,417
Total	1,681,689	779,343	933,718	3,394,750	173,194,247	176,588,997
Residential Real Estate:						
First mortgage	—	150,457	583,416	733,873	88,618,832	89,352,705
Second mortgage	68,332	48,321	—	116,653	11,931,784	12,048,437
HELOC	209,868	27,446	—	237,314	24,754,926	24,992,240
Total	278,200	226,224	583,416	1,087,840	125,305,542	126,393,382
Commercial:						
Agency secured	119,708	5,294	75,539	200,541	173,871,034	174,071,575
Agency unsecured	33,018	10,807	—	43,825	15,999,854	16,043,679
Real estate	—	—	631,909	631,909	108,980,139	109,612,048
Total	152,726	16,101	707,448	876,275	298,851,027	299,727,302
Grand Total	$2,112,615	$1,021,668	$2,224,582	$5,358,865	$597,350,816	$602,709,681

Loans on which the accrual of interest has been discontinued or reduced approximated $2,225,000 as of December 31, 2015. There were no loans 90 days or more past due and still accruing interest as of December 31, 2015.

Note 3 - Loans to Members (Continued)

Troubled Debt Restructurings

The income statement impact of approved TDRs was immaterial for financial statement disclosure for the year ended December 31, 2016 and 2015. Subsequently defaulted is defined as reaching 90 days past due during the first 12 months subsequent to approval.

The following table presents TDR activity by class of loans as of December 31, 2016:

	Number of Contracts	Recorded Investment in TDRs Approved	TDRs Which Subsequently Defaulted
Consumer:			
Unsecured			
Automobile	2	$40,472	$37,872
Residential Real Estate:			
First mortgage	2	457,353	454,097
Commercial:			
Real estate	2	1,004,758	981,495
Total	6	$1,502,583	$1,473,464

The following table presents TDR activity by class of loans as of December 31, 2015:

	Number of Contracts	Recorded Investment in TDRs Approved	TDRs Which Subsequently Defaulted
Consumer:			
Unsecured	9	$109,182	$96,827
Automobile	3	18,022	16,966
Residential Real Estate:			
First mortgage	1	151,286	149,489
Commercial:			
Real estate	2	1,498,402	1,482,588
Total	15	$1,776,892	$1,745,870

Note 3 - Loans to Members (Continued)

Consumer Credit Quality

The Credit Union considers the performance of the consumer loan portfolio and its impact on the allowance for loan losses. Consumer loan portfolio credit quality is evaluated based on the P360, Inc. risk grades as described in Note 1.

The following tables present the loan balance based on credit quality as of December 31, 2016 and 2015:

	2016			
Risk Grade	Other secured	Unsecured	Automobile	Total
V1	$—	$55,325,096	$80,238,885	$135,563,981
V2	—	19,819,650	1,487,580	21,307,230
V3	—	7,880,582	762,890	8,643,472
V4	—	4,157,872	241,277	4,399,149
V5	—	1,661,155	100,042	1,761,197
V6	—	723,479	85,690	809,169
V7	—	455,653	47,833	503,486
V8	—	318,077	141,352	459,429
V9	—	1,166,755	340,491	1,507,246
No risk grade	1,791,561	486,852	—	2,278,413
	$1,791,561	$91,995,171	$83,446,040	$177,232,772

	2015			
Risk Grade	Other secured	Unsecured	Automobile	Total
V1	$—	$51,968,885	$73,633,846	$125,602,731
V2	—	25,324,554	2,642,060	27,966,614
V3	—	8,679,692	1,215,943	9,895,635
V4	—	4,765,152	696,237	5,461,389
V5	—	1,655,969	336,482	1,992,451
V6	—	907,039	88,074	995,113
V7	—	604,304	167,255	771,559
V8	—	262,570	98,149	360,719
V9	—	1,083,140	154,954	1,238,094
No risk grade	1,967,418	337,274	—	2,304,692
	$1,967,418	$95,588,579	$79,033,000	$176,588,997

Note 3 - Loans to Members (Continued)

Real Estate Credit Quality

The Credit Union considers the performance of the real estate loan portfolio and its impact on the allowance for loan losses. Real estate loan portfolio credit quality is evaluated based on the P360, Inc. risk grades as described in Note 1.

The following tables present the loan balance based on credit quality as of December 31, 2016 and 2015:

	2016			
Risk Grade	First mortgage	Second mortgage	HELOC	Total
V1	$88,546,629	$13,541,148	$24,351,025	$126,438,802
V2	1,538,860	255,711	366,899	2,161,470
V3	368,037	412,889	24,070	804,996
V4	1,050,285	64,736	173,977	1,288,998
V5	89,338	94,324	136,371	320,033
V6	—	24,759	—	24,759
V7	—	47,215	—	47,215
V8	522,755	22,336	—	545,091
V9	—	—	—	—
No risk grade	103,614	—	—	103,614
	$92,219,518	$14,463,118	$25,052,342	$131,734,978

	2015			
Risk Grade	First mortgage	Second mortgage	HELOC	Total
V1	$85,584,932	$10,590,232	$24,273,277	$120,448,441
V2	583,402	703,815	344,980	1,632,197
V3	2,242,460	248,940	190,178	2,681,578
V4	192,621	254,742	142,843	590,206
V5	130,827	124,740	—	255,567
V6	302,909	22,977	13,516	339,402
V7	60,745	—	—	60,745
V8	137,874	102,991	—	240,865
V9	—	—	27,446	27,446
No risk grade	116,935	—	—	116,935
	$89,352,705	$12,048,437	$24,992,240	$126,393,382

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015

Note 3 - Loans to Members (Continued)

Commercial Credit Quality

The Credit Union considers the performance of the commercial loan portfolio and its impact on the allowance for loan losses. Commercial loan portfolio credit quality is evaluated based on the P360, Inc. risk grades as described in Note 1.

The following tables present the loan balance for commercial loans based on risk rating as of December 31, 2016 and 2015:

	2016			
Risk Grade	Agency secured	Agency unsecured	Real estate	Total
V1	$—	$11,361,104	$62,182,814	$73,543,918
V2	—	6,146,977	35,351,487	41,498,464
V3	—	3,807,726	14,386,038	18,193,764
V4	—	1,332,173	4,565,439	5,897,612
V5	—	796,917	2,156,967	2,953,884
V6	—	354,012	—	354,012
V7	—	143,001	344,634	487,635
V8	—	—	—	—
V9	—	91,965	288,543	380,508
No risk grade	183,342,450	—	—	183,342,450
	$183,342,450	$24,033,875	$119,275,922	$326,652,247

	2015			
Risk Grade	Agency Secured	Agency Unsecured	Real Estate	Total
V1	$—	$390,004	$60,230,410	$60,620,414
V2	—	5,232,893	24,516,576	29,749,469
V3	—	6,923,757	14,082,278	21,006,035
V4	—	345,710	2,968,468	3,314,178
V5	—	1,284,143	3,198,868	4,483,011
V6	—	499,029	775,119	1,274,148
V7	—	865,249	501,614	1,366,863
V8	—	394,286	—	394,286
V9	—	108,608	732,465	841,073
No risk grade	174,071,575	—	2,606,250	176,677,825
	$174,071,575	$16,043,679	$109,612,048	$299,727,302

Note 4 - Property and Equipment

Property and equipment is carried at cost, less accumulated depreciation and amortization, and are summarized as of December 31, 2016 and 2015 by major classification as follows:

	2016	2015
Furniture and equipment	$13,764,770	$10,990,988
Leasehold improvements	2,314,391	2,326,231
	16,079,161	13,317,219
Less accumulated depreciation and amortization	(12,266,457)	(11,172,078)
	$3,812,704	$2,145,141

Note 5 - Members' Shares and Savings Accounts

Members' shares and savings accounts are summarized as follows as of December 31, 2016 and 2015:

	2016	2015
Share accounts	$118,921,225	$114,244,496
Share draft accounts	120,285,032	107,576,202
Money market accounts	224,030,865	222,481,157
Individual retirement accounts	32,530,774	34,987,329
Share and IRA certificates	104,505,211	110,559,014
	$600,273,107	$589,848,198

As of December 31, 2016, scheduled maturities of share and IRA certificates are as follows:

	2016
Within one year	$64,991,733
1 to 2 years	16,745,701
2 to 3 years	6,673,602
3 to 4 years	9,126,632
4 to 5 years	6,967,543
	$104,505,211

Note 5 - Members' Shares and Savings Accounts (Continued)

The aggregate amount of members' time deposit accounts in denominations of $250,000 or more was approximately $10,564,000 as of December 31, 2016.

Note 6 - Borrowings

Lines of Credit

As of December 31, 2016 and 2015, the Credit Union maintained an unused line of credit with CCFCU. The terms of the agreement require the pledging of all presently owned and later acquired unencumbered assets as security for obligations under the line-of-credit agreement. The total unused line of credit under this agreement approximated $18,000,000 and $50,000,000 as of December 31, 2016 and 2015, respectively.

The Credit Union has entered into a credit availability agreement with UBS Bank USA which allows the Credit Union to borrow against its securities held in safekeeping. The total unused line of credit under this agreement was $7,742,000 and $8,854,000 as of December 31, 2016 and 2015, respectively.

The Credit Union maintains a credit availability agreement with the Federal Reserve Bank of San Francisco to comply with NCUA regulations Part 741.12: Maintaining Access to Emergency Liquidity. This credit availability agreement allows the Credit Union to borrow against its vehicle loan portfolio. The Credit Union is able to borrow according to the percentages published in the current "Federal Reserve Discount Window and Payment System Risk Collateral Margins Table" which is available on the Federal Reserve Bank's website. The total unused line of credit under this agreement was approximately $57,817,000 and $53,900,000 as of December 31, 2016 and 2015, respectively.

As a member of the FHLB, the Credit Union has access to a pre-approved secured line of credit with the capacity to borrow up to a certain percentage of the value of its eligible collateral, as defined in the FHLB Statement of Credit Policy. The agreement requires the pledging of eligible collateral for borrowing capacity. Based on the collateral pledged, the maximum available line of credit as of December 31, 2016 and 2015 was approximately $53,121,000 and $171,646,000, respectively, of which approximately $47,583,000 and $171,646,000 was available, respectively.

The advances outstanding are as follows as of December 31, 2016 and 2015:

Lender	Interest Type	Interest Rate	Final Maturity Date	Payment Type	2016	2015
FHLB	Fixed	1.45%	August 11, 2021	Non-amortizing	$5,537,894	$—

Note 7 - Employee Benefits

Retirement Plans

Credit Union management and staff are employed by the Credit Union's sponsor, Farmers and leased to the Credit Union. As such, Credit Union employees participate in Farmers pension plans and the Credit Union reimburses Farmers for pension plan expenses associated with the leased employees. On January 1, 2009, the Credit Union's defined benefit pension plan was modified and only vested employees who were age 40 and over, or who had 10 years of service as of December 31, 2008, were grandfathered into the existing pension plan. All remaining and new employees became participants of the Cash Balance Program. Farmers makes quarterly contributions to the employees' cash balance account, which is based on a percentage of the employees' salaries. Also, the Credit Union has a 401(k) plan through Farmers, which allows employees to defer a portion of their salary into the 401(k) plan up to certain limits established by the Internal Revenue Service. The Credit Union makes discretionary matching contributions each payroll period, with quarterly adjustments as needed. Participants are always 100% vested in all their voluntary contributions. The Credit Union's matching contributions become fully vested at the completion of three years of service.

Retirement plan costs are accrued and funded on a current basis. Total retirement plan costs paid by the Credit Union to Farmers for the years ended December 31, 2016 and 2015 amounted to approximately $1,714,000 and $1,439,000, respectively.

Note 8 - Commitments and Contingent Liabilities

Lease Commitments

The Credit Union leases several branch locations. The minimum non-cancellable lease obligations approximate the following as of December 31, 2016:

Year ending December 31,	Amount
2017	$1,060,000
2018	931,000
2019	820,000
2020	132,000
2021	94,000
Thereafter	666,000
	$3,703,000

Net rent expense under operating leases, included in expenses, was approximately $1,290,000 and $1,262,000 for the years ended December 31, 2016 and 2015, respectively.

Note 8 - Commitments and Contingent Liabilities (Continued)

Off Balance-Sheet Risk

The Credit Union is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its members and to reduce its own exposure to fluctuations in interest rates. These financial instruments include commitments to extend credit. These instruments involve, to varying degrees, elements of credit and interest-rate risk in excess of the amount recognized in the statements of financial condition.

Commitments to extend credit are agreements to lend to a member as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses. Since many of the commitments may expire without being fully drawn upon, the total commitment amounts do not necessarily represent future cash requirements. As of December 31, 2016, the total unfunded commitments under such lines of credit was approximately $194,107,000. The Credit Union evaluates each member’s creditworthiness on a case-by-case basis. The amount of collateral obtained, if any, is based on management’s credit evaluation of the member.

Note 9 - Regulatory Capital

The Credit Union is subject to various regulatory capital requirements administered by the NCUA. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Credit Union’s financial statements. Under capital adequacy regulations and the regulatory framework for prompt corrective action, the Credit Union must meet specific capital regulations that involve quantitative measures of the Credit Union’s assets, liabilities, and certain off-balance-sheet items as calculated under generally accepted accounting practices. The Credit Union’s capital amounts and net worth classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Credit Union to maintain minimum amounts and ratios (set forth in the table below) of net worth (as defined in *NCUA Regulations*) to total assets (as defined in *NCUA Regulations*). Credit unions are also required to calculate a Risk-Based Net Worth Requirement (RBNWR) which establishes whether or not the Credit Union will be considered “complex” under the regulatory framework. The Credit Union’s RBNWR as of December 31, 2016 and 2015 was 7.03% and 6.62%, respectively. The minimum requirement to be considered complex under the regulatory framework is 6.00%. Management believes, as of December 31, 2016 and 2015, that the Credit Union meets all capital adequacy requirements to which it is subject.

Note 9 - Regulatory Capital (Continued)

As of December 31, 2016, the most recent call reporting period, the NCUA categorized the Credit Union as *"well capitalized"* under the regulatory framework for prompt corrective action. To be categorized as *"well capitalized"* the Credit Union must maintain a minimum net worth ratio of 7.00% of assets. There are no conditions or events since that notification that management believes have changed the Credit Union's category.

The Credit Union's actual and required net worth amounts and ratios are as follows:

	As of December 31, 2016		As of December 31, 2015	
	Amount	Ratio/ Requirement	Amount	Ratio/ Requirement
Actual net worth	$99,958,770	14.03%	$93,896,443	13.59%
Amount needed to meet the minimum RBNW requirement	$50,081,751	7.03%	$45,741,126	6.62%
Amount needed to be classified as "well capitalized"	$49,868,030	7.00%	$48,366,749	7.00%
Amount needed to be classified as "adequately capitalized"	$42,744,026	6.00%	$41,457,213	6.00%

Because the RBNWR is less than the net worth ratio, the Credit Union retains its original category. Further, in performing its calculation of total assets, the Credit Union used the quarter end option, as permitted by regulation.

Note 10 - Fair Value Measurements

Accounting standards establish a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under this guidance are described below.

Basis of Fair Value Measurements

Level 1 - Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Credit Union has the ability to access at the measurement date. An active market for the asset or liability is a market in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis.

Note 10 - Fair Value Measurements (Continued)

Level 2 - Valuation is based on inputs other than quoted market prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. The valuation may be based on quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.

Level 3 - Valuation is generated from model-based techniques use at least one significant assumption not observable in the market. Level 3 assets and liabilities include financial instruments whose value is determined by using pricing models, discounted cash flow methodologies, or similar techniques.

Assets Measured at Fair Value on a Recurring Basis

Assets measured at fair value on a recurring basis are summarized as follows:

	Assets at Fair Value as of December 31, 2016			
	Level 1	**Level 2**	**Level 3**	**Total**
Available-for-sale:				
Mortgage-backed securities	$—	$1,397,209	$—	$1,397,209
NCUA guaranteed notes	—	8,148,451	—	8,148,451
Collateralized mortgage obligations	—	18,416	—	18,416
	$—	$9,564,076	$—	$9,564,076

	Assets at Fair Value as of December 31, 2015			
	Level 1	**Level 2**	**Level 3**	**Total**
Available-for-sale:				
Mortgage-backed securities	$—	$1,711,820	$—	$1,711,820
NCUA guaranteed notes	—	11,028,015	—	11,028,015
Collateralized mortgage obligations	—	23,951	—	23,951
	$—	$12,763,786	$—	$12,763,786

Note 10 - Fair Value Measurements (Continued)

Assets Measured at Fair Value on a Non-Recurring Basis

Impaired Loans

Loans for which the Credit Union has measured impairment are generally based on the fair value of the loan's collateral. Fair value is generally determined based upon independent third-party appraisals of the properties, or discounted cash flows based upon the expected proceeds. These assets are included as Level 3 fair values, based upon the lowest level of input that is significant to the fair value measurements. The fair value consists of the loan balances less the valuation allowance and/or charge-offs.

Assets measured at fair value on a non-recurring basis:

	Assets at Fair Value as of December 31, 2016			
	Level 1	**Level 2**	**Level 3**	**Total**
Impaired loans	$—	$—	$11,727,203	$11,727,203

	Assets at Fair Value as of December 31, 2015			
	Level 1	**Level 2**	**Level 3**	**Total**
Impaired loans	$—	$—	$10,990,091	$10,990,091

Note 11 - Related Party Transactions

Loans

In the ordinary course of business, the Credit Union grants loans to certain directors and executive officers. Such loans aggregated approximately $2,455,000 and $2,521,000 as of December 31, 2016 and 2015, respectively.

Deposits

Deposits of Credit Union directors and executive officers were approximately $2,556,000 and $1,906,000 as of December 31, 2016 and 2015, respectively.

* * * End of Notes * * *

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