

STAYING THE COURSE



FARMERS INSURANCE
FEDERAL
CREDIT UNION

2022 Annual Report

2022

Highlights

Total Net Loans



\$1,279,927,758

\$1,014,386,528

\$950,199,833

Membership Shares

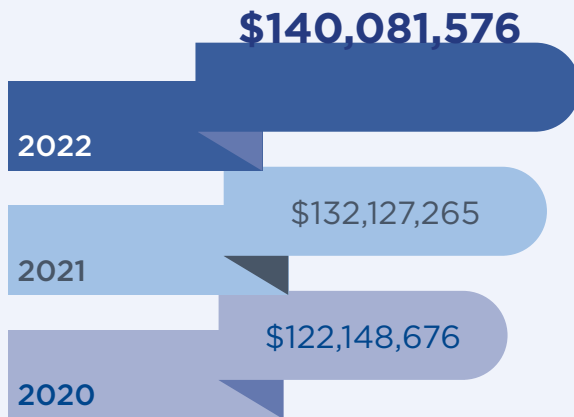


\$1,131,282,668

\$1,055,358,867

\$988,681,647

Retained Earnings

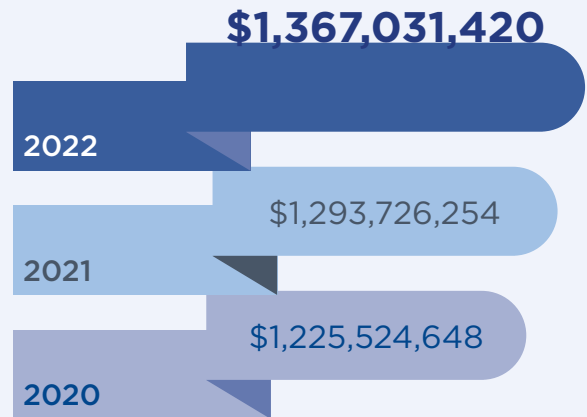


\$140,081,576

\$132,127,265

\$122,148,676

Total Assets



\$1,367,031,420

\$1,293,726,254

\$1,225,524,648

Net Income



\$7,954,311

2021 \$9,978,589

2020 \$4,310,101

Total Members



59,091

2021 60,270

2020 57,534



NPS Score

83.02%

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

FINANCIAL STATEMENTS

DECEMBER 31, 2022 AND 2021

(With Independent Auditor's Report Thereon)

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

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Independent Auditor's Report

April 11, 2023

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

Report on the Audits of the Financial Statements

Opinion

We have audited the financial statements of Farmers Insurance Group Federal Credit Union (the Credit Union), which comprise the statements of financial condition as of December 31, 2022 and 2021, 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.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Credit Union as of December 31, 2022 and 2021, 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 (GAAP).

Basis for Opinion

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

Emphasis of Matter - Change in Accounting Principle

As discussed in Note 1 to the financial statements, the entity adopted the new lease standard during the year ended December 31, 2022. Our opinion is not modified with respect to this matter.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with GAAP, and for 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.

To the Supervisory Committee and Board of Directors
and Management of Farmers Insurance Group Federal Credit Union
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Report on the Audits of the Financial Statements (Continued)

Responsibilities of Management for the Financial Statements (Continued)

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

Auditor's Responsibilities for the Audits of the Financial Statements

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

In performing audits in accordance with GAAS, we:

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

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

Doeren Mayhew

Doeren Mayhew
Miami, FL

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF FINANCIAL CONDITION AS OF DECEMBER 31, 2022 AND 2021

	2022	2021
<u>Assets</u>		
Cash and cash equivalents	\$34,701,730	\$120,295,674
Interest bearing deposits	1,245,000	43,967,997
Investment securities (Note 2):		
Equity	—	69,724,599
Available-for-sale	306,423	393,731
Credit Union Service Organizations (CUSO)	9,749,095	15,343,171
Federal Home Loan Bank (FHLB) stock	3,568,800	2,983,900
Loans to members, net of allowance for loan losses (Note 3)	1,279,927,758	1,014,386,528
Accrued interest receivable	5,800,183	4,801,669
Prepaid and other assets	18,304,924	7,716,224
Property and equipment (Note 4)	3,288,175	4,304,705
National Credit Union Share Insurance Fund (NCUSIF) deposit	10,139,332	9,808,056
	\$1,367,031,420	\$1,293,726,254
Total assets		
<u>Liabilities and Members' Equity</u>		
Liabilities:		
Members' shares and savings accounts (Note 5)	\$1,131,282,668	\$1,055,358,867
Borrowed funds (Note 6)	74,650,000	94,948,195
Accrued expenses and other liabilities	21,024,785	11,279,899
	1,226,957,453	1,161,586,961
Total liabilities		
Commitments and contingent liabilities		
Members' equity:		
Regular reserve	—	16,966,743
Undivided earnings	140,081,576	115,160,522
Accumulated other comprehensive (loss)/income	(7,609)	12,028
	140,073,967	132,139,293
Total members' equity		
Total liabilities and members' equity	\$1,367,031,420	\$1,293,726,254

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF INCOME YEARS ENDED DECEMBER 31, 2022 AND 2021

	2022	2021
Interest income:		
Loans to members	\$64,797,259	\$57,193,050
Investment securities	2,014,800	787,197
Total interest income	66,812,059	57,980,247
Interest expense:		
Members' shares and savings accounts	8,436,178	7,446,282
Borrowed funds	1,674,688	1,966,729
Total interest expense	10,110,866	9,413,011
Net interest income	56,701,193	48,567,236
Provision for loan losses	10,886,952	1,487,214
Net interest income after provision for loan losses	45,814,241	47,080,022
Non-interest income:		
Overdraft and share draft fees	2,977,304	2,547,317
Interchange income	4,148,658	3,895,464
Service charges and other fees	1,098,371	1,022,673
Gain on sale of CUSO (Note 1)	2,729,054	—
Other income	353,313	323,034
Total non-interest income	11,306,700	7,788,488
Non-interest expenses:		
Compensation and benefits	28,822,655	25,278,644
Office operating costs	9,625,284	9,007,389
Educational and promotional	1,082,335	2,146,085
Professional and outside services	2,396,581	1,999,386
Office occupancy	1,808,023	1,931,432
Other expenses	2,602,676	2,726,441
Loan servicing	2,829,076	1,800,544
Total non-interest expenses	49,166,630	44,889,921
Net income	\$7,954,311	\$9,978,589

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF COMPREHENSIVE INCOME YEARS ENDED DECEMBER 31, 2022 AND 2021

	<u>2022</u>	<u>2021</u>
Net income	\$7,954,311	\$9,978,589
Other comprehensive loss:		
Available-for-sale investment securities:		
Net unrealized holding losses on available-for-sale investment securities	(19,637)	(1,492)
Other comprehensive loss	(19,637)	(1,492)
Comprehensive income	<u>\$7,934,674</u>	<u>\$9,977,097</u>

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF MEMBERS' EQUITY YEARS ENDED DECEMBER 31, 2022 AND 2021

	Regular Reserve	Undivided Earnings	Accumulated Other Comprehensive Income/(Loss)	Total
Balance, December 31, 2020	\$16,966,743	\$105,181,933	\$13,520	\$122,162,196
Net income	—	9,978,589	—	9,978,589
Other comprehensive loss	—	—	(1,492)	(1,492)
Balance, December 31, 2021	16,966,743	115,160,522	12,028	132,139,293
Net income	—	7,954,311	—	7,954,311
Other comprehensive loss	—	—	(19,637)	(19,637)
Transfer (Note 1)	(16,966,743)	16,966,743	—	—
Balance, December 31, 2022	\$—	\$140,081,576	(\$7,609)	\$140,073,967

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2022 AND 2021

	<u>2022</u>	<u>2021</u>
Cash flows from operating activities:		
Net income	\$7,954,311	\$9,978,589
Adjustments to net cash provided from operating activities:		
Provision for loan losses	10,886,952	1,487,214
Net loss on equity investment securities	—	522,497
Loss attributable to investments in CUSOs	1,353,048	592,549
Gain on sale of CUSO	(2,729,054)	—
Depreciation and amortization	1,580,137	1,640,352
(Increase)/decrease in:		
Accrued interest receivable	(998,514)	834,366
Prepaid and other assets	(1,972,950)	(1,793,221)
Increase/(decrease) in:		
Accrued expenses and other liabilities	1,129,136	1,728,080
Total adjustments	9,248,755	5,011,837
Net cash provided from operating activities	17,203,066	14,990,426

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2022 AND 2021

Cash Flows (Continued)

	2022	2021
Cash flows from investing activities:		
Proceeds from interest bearing deposits	43,469,997	—
Purchase of interest bearing deposits	(747,000)	(6,575,004)
Proceeds from equity investment securities	69,724,599	69,752,904
Purchase of equity investment securities	—	(140,000,000)
Proceeds from maturities and repayments of available-for-sale investment securities	67,671	1,072,677
Investment in CUSOs	(400,000)	—
Proceeds from the sale of CUSO	4,370,082	—
Decrease in loans to CUSO	3,000,000	—
Purchase of FHLB stock	(584,900)	—
Net change in loans to members	(276,428,182)	(65,673,909)
Expenditures for property and equipment	(563,607)	(1,328,976)
Increase in NCUSIF deposit	(331,276)	(237,609)
	(158,422,616)	(142,989,917)
Cash flows from financing activities:		
Net change in members' shares and savings accounts	75,923,801	66,677,220
Repayment of borrowed funds	(20,298,195)	(10,180,791)
	55,625,606	56,496,429
Net change in cash and cash equivalents	(85,593,944)	(71,503,062)
Cash and cash equivalents - beginning	120,295,674	191,798,736
Cash and cash equivalents - ending	\$34,701,730	\$120,295,674

Supplemental Information

Interest paid	\$10,110,866	\$9,413,011
Lease liabilities arising from obtaining right-of-use assets	\$8,615,750	\$—

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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 (GAAP) 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 and the fair value of financial instruments. 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.

Comprehensive Income/(Loss)

Accounting principles generally require that 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 in the statements of income.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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

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. Time deposits with banks and corporate credit unions may, at times, exceed federally insured limits.

Investment Securities

The Credit Union's investment securities are classified and accounted for as follows:

Equity: Securities have readily determinable fair values. Equity securities are recorded at fair value with unrealized gains and losses, due to changes in fair value, reflected in earnings. Unrealized and realized gains and losses are recognized in net gains/(losses) from equity securities in the statements of income. Dividend income from marketable equity securities is recognized in interest income.

Available-for-Sale: Debt securities are classified as available-for-sale when the Credit Union anticipates that the securities could be sold in response to rate changes, prepayment risk, liquidity, availability of and the yield on alternative investments and other market and economic factors. These securities are reported at fair value in the statements of financial conditions.

Unrealized gains and losses on available-for-sale debt securities are recognized as direct increases or decreases in other comprehensive income/(loss). Premiums and discounts are recognized in interest income over the terms of the securities. Declines in the estimated fair value of available-for-sale debt securities 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: (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near term prospects of the issuer, (3) that the Credit Union does not intend to sell these securities, and (4) 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. Gains and losses on the sale of securities are recorded on the trade date and the costs of securities sold are determined using the specific identification method.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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

Credit Union Service Organizations

The Credit Union has investments in several credit union service organizations (CUSOs). As of December 31, 2022 and 2021, the Credit Union owned 50% of Community Mortgage Funding, LLC (CMF). CMF provides residential mortgage origination, processing, underwriting, closing, funding, and servicing for the benefit of credit unions. As of December 31, 2022, CMF's assets and liabilities approximated \$15,673,000 and \$8,260,000, respectively. As of December 31, 2021, CMF's assets and liabilities approximated \$21,641,000 and \$14,308,000, respectively. CMF reported net income of approximately \$172,000 and \$617,000 during the years ended December 31, 2022 and 2021, respectively. Additionally, the Credit Union has provided CMF a line of credit of \$4,000,000 and \$7,000,000 to facilitate CMF's operations during the years ended December 31, 2022 and 2021, respectively. The line of credit is secured by CMF's cash, receivables and intangible assets. The line of credit is variable rate and matures on June 17, 2023. As of December 31, 2022 and 2021, the outstanding balance of the line of credit was approximately \$4,000,000 and \$7,000,000, respectively.

As of December 31, 2022 and 2021, the Credit Union also owned 12.16% and 12.25%, respectively, of Constellation Digital Partners, LLC (CDP). CDP provides a cloud-based marketplace that enables credit unions and developers to provide digital financial services to credit union members. As of December 31, 2022, CDP's assets and liabilities approximated \$18,401,000 and \$10,923,000, respectively. As of December 31, 2021, CDP's assets and liabilities approximated \$19,621,000 and \$1,566,000, respectively. CDP reported net losses of approximately (\$10,679,000) and (\$12,211,000) during the years ended December 31, 2022 and 2021, respectively.

As of December 31, 2022 and 2021, the Credit Union also owned 0.79% and 9.10%, respectively, of Curql Fund I, LLLP (Curql). Curql was formed on October 20, 2020 by Curql Collective, LLC (the "Lead General Partner") and Next Level Ventures GP III LLC (the "Co-General Partner"). Curql's aim is to invest in fintech startups that provide technologies to improve credit union and credit union affiliate operations. Curql was established on March 29, 2021 as a cooperative Credit Union Service Organization.

The Lead General Partner supports collaboration between credit unions and fintech companies to establish a fintech ecosystem that benefits both parties. The Co-General Partner manages Curql's activities. A limited partnership agreement defines Curql's structure and activities (the "LPA"). The LPA gives the Lead General Partner and Co-General Partners joint authority and responsibility for managing the Fund. Curql's limited partners are credit unions, credit union affiliates, and CUSOs.

All of these investments are accounted for under the equity method based on the Credit Union's percentage of ownership and/or level of influence exercised over the companies. Under the equity method, initial investments are subsequently adjusted for the Credit Union's share of earnings and losses.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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

Credit Union Service Organizations (Continued)

As of December 31, 2021, the Credit Union also owned 2.67% of CU Railz, LLC (CU Railz). CU Railz offers an enhancement to the Credit Union's electronic bill pay platform and allows members to easily make payments to/from other financial institutions. The investment in CU Railz was accounted for under the cost method based on the Credit Union's percentage of ownership and/or level of influence exercised over the company. Under the cost method, the investment was recorded at its historical cost unless there was evidence of impairment. During the year ended December 31, 2022, the Credit Union sold its entire ownership interest in CU Railz. Proceeds from the sale approximated \$4,370,000, resulting in the Credit Union recognizing a gain of approximately \$2,729,000, during the year ended December 31, 2022.

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.

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

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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

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.

Agency secured loans are secured by the value of agencies owned by a Farmers Insurance Agent or a Farmers Insurance District Manager. Agency unsecured loans are comprised of unsecured loans used for agency acquisitions by Farmers Insurance Agents and other agency business purposes. Each class of loans requires significant judgment to determine 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.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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 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 (TDR) 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.

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.

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.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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

Allowance for Loan Losses (Continued)

Residential Real Estate Segment Allowance Methodology (Continued)

In addition, the allowance model incorporates numerous other historical factors based upon the borrower, collateral type, loan performance, environment, and economy. The 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. The historical factors used in the analysis date back to 2001.

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 agency 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.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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

Allowance for Loan Losses (Continued)

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 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.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Credit Union does not separately identify individual consumer and residential loans for impairment disclosures, unless such loans are the subject of a restructuring agreement.

Troubled Debt Restructurings (TDRs)

Under certain circumstances, the Credit Union will provide borrowers relief through loan restructurings. A loan restructuring represents a 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.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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

Allowance for Loan Losses (Continued)

Credit Quality Indicators (Continued)

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.

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.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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

Allowance for Loan Losses (Continued)

Credit Quality Indicators (Continued)

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.

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 10 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 15 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 20 percent of the loan balance.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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

Allowance for Loan Losses (Continued)

Credit Quality Indicators (Continued)

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 30 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 30 and 40 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.

V9 - Inherent loss - Assets in this risk area have an inherent value at risk, north of 40 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. Loans are generally charged off when the loan has been delinquent for 180 days. Management will monitor loans and if a loan is deemed uncollectable, where additional collection efforts are non-productive regardless of the number of days delinquent, the loan could be charged off at that time.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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

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.

Leases

The Credit Union recognizes right-of-use assets and lease liabilities for leases with terms greater than 12 months. Leases are classified as either finance or operating leases. This classification dictates whether lease expense is recognized based on an effective interest method (finance leases) or on a straight-line basis over the term of the lease (operating leases). Lease and non-lease components of a contract are accounted for as a single lease component. The Credit Union's right-of-use assets and lease liabilities primarily relate to office facilities, branches, and equipment used in connection with long-term contracts. Renewal periods are included in the expected lease term if they are reasonably certain of being exercised.

Right-of-use assets and lease liabilities are recorded at the net present value of future lease payments and include any initial direct costs incurred at lease commencement. The Credit Union has elected to use a risk-free discount rate to determine the net present value of the lease when the rate implicit in the lease is not readily determinable. Right-of-use assets under finance leases are amortized over the life of the lease or, if shorter, the life of the leased asset, on a straight-line basis. Right-of-use assets under operating leases are reduced as lease expense is incurred.

Short-term leases (initial terms less than 12 months) are expensed on a straight-line basis over the lease term. Right-of-use assets were approximately \$7,580,000 as of December 31, 2022 and are included within prepaid and other assets in the statements of financial condition. Lease liabilities were approximately \$7,694,000 as of December 31, 2022 and are included within accrued expenses and other liabilities in the statements of financial condition.

Perpetual Contributed Capital (PCC)

As a requirement of membership, the Credit Union maintains a PCC account with Catalyst Corporate Federal Credit Union (CCFCU) of \$600,000. The PCC is not subject to share insurance coverage. 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 non-cumulative dividend. The PCC is included within prepaid and other assets in the statements of financial condition.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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

National Credit Union Share Insurance Fund (NCUSIF) Deposit

The deposit in the NCUSIF is in accordance with National Credit Union Administration (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.

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 number 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.

Borrowed Funds

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

As of December 31, 2021, the Credit Union was required to maintain a statutory reserve (regular reserve) in accordance with the Federal Credit Union Act. This statutory reserve represented a regulatory restriction and was not available for the payment of interest. The regular reserve requirement was eliminated on January 1, 2022. The balance of \$16,966,743 was transferred to undivided earnings during the year ended December 31, 2022.

Revenue from Contracts with Customers

The Credit Union's revenue in the scope of ASC 606, Revenue from Contracts with Customers, is recognized and disaggregated within non-interest income in the statements of income. A description of the Credit Union's revenue streams accounted for under ASC 606 are as follows.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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

Revenue from Contracts with Customers (Continued)

Overdraft and Share Draft Fees, Service Charges and Other Fees

Fees and charges include charges related to depository accounts under standard service agreements (e.g., courtesy pay fees, insufficient funds charges, late fees, etc.). Transaction-based fees are recognized at the time of transaction which is the point in time the Credit Union fulfills the member's request. Other account maintenance fees are generally earned over the course of a month which is the period the Credit Union satisfies its performance obligation.

Interchange Income

Interchange income includes interchange fees from credit and debit cards processed through card association networks. The Credit Union earns a percentage of the underlying value of each transaction. These fees are recognized daily when the processing service is provided to the member. The costs of related loyalty rewards programs are presented separately in non-interest expenses in the statements of income.

Advertising Costs

Advertising costs are expensed as incurred and are reported as Educational and Promotional expenses in the statements of income.

Income Taxes

The Credit Union is exempt, by the Internal Revenue Code Section 501(c)(1)(a)(I), from federal and state income taxes.

Recent Accounting Pronouncements

Accounting for Financial Instruments - Credit Losses

In June 2016, the FASB issued Accounting Standards Update (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 debt 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.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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

Recent Accounting Pronouncements (Continued)

Accounting for Financial Instruments - Credit Losses (Continued)

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 the Credit Union on January 1, 2023. The initial entry to adopt CECL is approximately \$11,274,000 to be booked on adoption.

Adoption of Accounting Standards

On January 1, 2022, the Credit Union adopted ASU 2016-02, Leases and subsequent amendments thereto, which requires the Credit Union to recognize most leases in the statements of financial condition. The Credit Union adopted the standard under a modified retrospective approach as of the date of adoption and elected to apply several of the available practical expedients, including:

- Carry over of historical lease determination and lease classification conclusions
- Carry over of historical initial direct cost balances for existing leases
- Accounting or lease and non-lease components in contracts in which the Credit Union is a lessee as a single lease component.

Adoption of the lease standard resulted in the recognition of operating right-of-use assets and operating lease liabilities of approximately \$8,616,000 as of January 1, 2022. These amounts were determined based on the present value of remaining minimum lease payments, discounting using the risk-free discount rate as of the date of adoption. There was no material impact to the timing of expense or income recognition in the Credit Union's statements of income. Prior periods were not restated and continue to be presented under legacy GAAP. Disclosures about the Credit Union's leasing activities are presented in Note 8.

Reclassification

Certain amounts reported in the 2021 financial statements have been reclassified to conform with the 2022 presentation. Reclassification adjustments did not affect total members' equity or net income.

Subsequent Events

Management has evaluated subsequent events through April 11, 2023, the date the financial statements were available to be issued.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

Note 2 - Investment Securities

The estimated fair values of equity securities are as follows:

	As of December 31,	
	2022	2021
Mutual fund	\$—	\$69,724,599

The following table presents the amortized cost and estimated fair value of debt securities as of December 31, 2022:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
Mortgage-backed securities	\$314,032	\$—	(\$7,609)	\$306,423

The following table presents the amortized cost and estimated fair value of debt securities as of December 31, 2021:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
Mortgage-backed securities	\$381,703	\$12,028	\$—	\$393,731

As of December 31, 2022, the Credit Union's investment portfolio consisted entirely of mortgage-backed securities and collateralized mortgage obligations. These securities return principal based on payments received on the underlying mortgages or assets. These securities have expected weighted average lives ranging from two to seven years. However, return of principal may differ from expectation based on fluctuations in market interest rates, delinquency, foreclosures and the underlying collateral values. Additionally, borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

Note 2 - Investment Securities (Continued)

Information pertaining to investments with gross unrealized losses as of December 31, 2022, aggregated by investment category and length of time that individual investments have been in a continuous loss position follows:

	<u>Less than 12 Months</u>		<u>12 Months or Longer</u>		<u>Total</u>	
	Gross		Gross		Gross	
	Fair	Unrealized	Fair	Unrealized	Fair	Unrealized
	Value	Losses	Value	Losses	Value	Losses
Available-for-sale:						
Mortgage-backed securities	\$306,423	(\$7,609)	\$—	\$—	\$306,423	(\$7,609)

Unrealized losses on securities issued by the U.S. Government and its Agencies have not been recognized into income because of 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.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

Note 3 - Loans to Members

The composition of loans to members as of December 31, 2022 and 2021 is as follows:

	2022	2021
Consumer:		
Unsecured	\$107,145,694	\$104,228,472
Automobile	114,863,285	96,625,652
Other secured	1,546,110	1,819,688
	223,555,089	202,673,812
Residential Real Estate:		
First mortgage	278,262,045	201,123,650
Second mortgage	63,518,023	29,278,342
HELOC	43,133,398	27,242,121
	384,913,466	257,644,113
Commercial:		
Agency secured	219,088,800	214,394,280
Agency unsecured	198,039,984	162,455,303
Real estate	260,639,852	180,437,730
	677,768,636	557,287,313
Total loans	1,286,237,191	1,017,605,238
Deferred loan origination fees/costs, net	3,983,815	3,685,958
	1,290,221,006	1,021,291,196
Less: Allowance for loan losses	(10,293,248)	(6,904,668)
Loans to members, net	\$1,279,927,758	\$1,014,386,528

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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, 2022:

	Consumer	Residential Real Estate	Commercial	Total
Allowance for loan losses:				
Beginning allowance	\$3,146,448	\$1,017,347	\$2,740,873	\$6,904,668
Charge-offs	(5,659,755)	(7,115)	(3,946,570)	(9,613,440)
Recoveries	1,829,228	—	285,840	2,115,068
Provision for loan losses	5,926,158	39,194	4,921,600	10,886,952
Ending allowance	<u>\$5,242,079</u>	<u>\$1,049,426</u>	<u>\$4,001,743</u>	<u>\$10,293,248</u>
Ending balance individually evaluated for impairment	\$22	\$585,005	\$—	\$585,027
Ending balance collectively evaluated for impairment	<u>5,242,057</u>	<u>464,421</u>	<u>4,001,743</u>	<u>9,708,221</u>
Ending allowance	<u>\$5,242,079</u>	<u>\$1,049,426</u>	<u>\$4,001,743</u>	<u>\$10,293,248</u>

The following table presents a summary of the recorded investment in loans by portfolio segment as of December 31, 2022:

	Consumer	Residential Real Estate	Commercial	Total
Loans:				
Ending balance individually evaluated for impairment	\$174,958	\$5,315,995	\$—	\$5,490,953
Ending balance collectively evaluated for impairment	<u>223,926,911</u>	<u>382,612,079</u>	<u>678,191,063</u>	<u>1,284,730,053</u>
Total loans	<u>\$224,101,869</u>	<u>\$387,928,074</u>	<u>\$678,191,063</u>	<u>\$1,290,221,006</u>

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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, 2021:

	Consumer	Residential Real Estate	Commercial	Total
Allowance for loan losses:				
Beginning allowance	\$3,526,050	\$2,237,844	\$3,283,886	\$9,047,780
Charge-offs	(2,907,590)	—	(2,012,333)	(4,919,923)
Recoveries	1,171,306	988	117,303	1,289,597
Provision for loan losses	1,356,682	(1,221,485)	1,352,017	1,487,214
Ending allowance	<u>\$3,146,448</u>	<u>\$1,017,347</u>	<u>\$2,740,873</u>	<u>\$6,904,668</u>
Ending balance individually evaluated for impairment	\$13,168	\$584,351	\$—	\$597,519
Ending balance collectively evaluated for impairment	<u>3,133,280</u>	<u>432,996</u>	<u>2,740,873</u>	<u>6,307,149</u>
Ending allowance	<u>\$3,146,448</u>	<u>\$1,017,347</u>	<u>\$2,740,873</u>	<u>\$6,904,668</u>

The following table presents a summary of the recorded investment in loans by portfolio segment as of December 31, 2021:

	Consumer	Residential Real Estate	Commercial	Total
Loans:				
Ending balance individually evaluated for impairment	\$315,575	\$5,347,982	\$79,892	\$5,743,449
Ending balance collectively evaluated for impairment	<u>202,683,007</u>	<u>254,738,789</u>	<u>558,125,951</u>	<u>1,015,547,747</u>
Total loans	<u>\$202,998,582</u>	<u>\$260,086,771</u>	<u>\$558,205,843</u>	<u>\$1,021,291,196</u>

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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, 2022:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
<u>With no allowance recorded:</u>					
Residential Real Estate:					
Second mortgage	\$181,784	\$181,784	\$—	\$181,784	\$10,990
<u>With an allowance recorded:</u>					
Consumer:					
Unsecured	\$105,641	\$105,641	\$19	\$162,361	\$16,885
Automobile	\$69,317	\$69,317	\$3	\$82,906	\$2,893
Residential Real Estate:					
First mortgage	\$5,031,913	\$4,957,911	\$543,504	\$5,143,995	\$210,904
HELOC	\$102,299	\$102,306	\$41,501	\$102,299	\$8,133
Totals by loan segment:					
Consumer	\$174,958	\$174,958	\$22	\$245,267	\$19,778
Residential Real Estate	5,315,996	5,242,001	585,005	5,428,078	230,027
Total	<u>\$5,490,954</u>	<u>\$5,416,959</u>	<u>\$585,027</u>	<u>\$5,673,345</u>	<u>\$249,805</u>

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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, 2021:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
<u>With no allowance recorded:</u>					
Commercial:					
Agency unsecured	\$79,892	\$79,891	\$—	\$—	\$—
Residential Real Estate:					
Second mortgage	\$91,905	\$91,905	\$—	\$—	\$—
<u>With an allowance recorded:</u>					
Consumer:					
Unsecured	\$219,080	\$219,080	\$9,278	\$245,655	\$24,664
Automobile	\$96,495	\$96,495	\$3,890	\$55,291	\$1,825
Residential Real Estate:					
First mortgage	\$5,256,077	\$5,193,553	\$584,351	\$5,286,659	\$197,192
Totals by loan segment:					
Consumer	\$315,575	\$315,575	\$13,168	\$300,946	\$26,489
Residential Real Estate	5,347,982	5,285,458	584,351	5,286,659	197,192
Commercial	79,892	79,891	—	—	—
Total	<u>\$5,743,449</u>	<u>\$5,680,924</u>	<u>\$597,519</u>	<u>\$5,587,605</u>	<u>\$223,681</u>

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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, 2022:

	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Current	Total loans
Consumer:						
Unsecured	\$1,286,062	\$759,522	\$1,504,439	\$3,550,023	\$104,142,451	\$107,692,474
Automobile	558,920	171,915	156,366	887,201	113,976,084	114,863,285
Other secured	63,489	—	5,305	68,794	1,477,316	1,546,110
Total	1,908,471	931,437	1,666,110	4,506,018	219,595,851	224,101,869
Residential Real Estate:						
First mortgage	2,282,160	875,779	1,484,438	4,642,377	276,324,825	280,967,202
Second mortgage	224,972	60,147	121,637	406,756	63,423,787	63,830,543
HELOC	426,022	13,907	88,392	528,321	42,602,008	43,130,329
Total	2,933,154	949,833	1,694,467	5,577,454	382,350,620	387,928,074
Commercial:						
Agency secured	248,760	694	290,721	540,175	218,548,649	219,088,824
Agency unsecured	1,014,837	307,274	944,162	2,266,273	195,638,663	197,904,936
Real estate	49,940	—	—	49,940	261,147,363	261,197,303
Total	1,313,537	307,968	1,234,883	2,856,388	675,334,675	678,191,063
Grand Total	\$6,155,162	\$2,189,238	\$4,595,460	\$12,939,860	\$1,277,281,146	\$1,290,221,006

Loans on which the accrual of interest has been discontinued or reduced approximated \$4,595,000 as of December 31, 2022. There were no loans 90 days or more past due and still accruing interest as of December 31, 2022.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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, 2021:

	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Current	Total Loans
Consumer:						
Unsecured	\$788,210	\$456,493	\$884,706	\$2,129,409	\$102,423,833	\$104,553,242
Automobile	304,741	116,151	156,026	576,918	96,048,734	96,625,652
Other secured	36,030	—	—	36,030	1,783,658	1,819,688
Total	1,128,981	572,644	1,040,732	2,742,357	200,256,225	202,998,582
Residential Real Estate:						
First mortgage	3,596,712	839,471	3,427,812	7,863,995	195,706,845	203,570,840
Second mortgage	325,301	58,974	32,930	417,205	28,861,137	29,278,342
HELOC	370,412	—	—	370,412	26,867,177	27,237,589
Total	4,292,425	898,445	3,460,742	8,651,612	251,435,159	260,086,771
Commercial:						
Agency secured	444,179	264,154	406,666	1,114,999	213,254,213	214,369,212
Agency unsecured	954,902	520,741	1,143,338	2,618,981	159,399,682	162,018,663
Real estate	118,933	—	1,556,552	1,675,485	180,142,483	181,817,968
Total	1,518,014	784,895	3,106,556	5,409,465	552,796,378	558,205,843
Grand Total	\$6,939,420	\$2,255,984	\$7,608,030	\$16,803,434	\$1,004,487,762	\$1,021,291,196

Loans on which the accrual of interest has been discontinued or reduced approximated \$7,608,000 as of December 31, 2021. There were no loans 90 days or more past due and still accruing interest as of December 31, 2021.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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 recorded investment in consumer loans based on credit quality as of December 31, 2022 and 2021:

Risk Grade	2022			
	Other Secured	Unsecured	Automobile	Total
V1	\$1,546,110	\$69,962,480	\$111,108,756	\$182,617,346
V2	—	14,945,197	2,393,515	17,338,712
V3	—	10,441,626	526,099	10,967,725
V4	—	6,089,118	293,690	6,382,808
V5	—	1,370,964	180,664	1,551,628
V6	—	836,320	47,134	883,454
V7	—	758,674	88,511	847,185
V8	—	381,169	71,425	452,594
V9	—	2,458,105	153,187	2,611,292
No risk grade	—	448,821	304	449,125
	\$1,546,110	\$107,692,474	\$114,863,285	\$224,101,869

Risk Grade	2021			
	Other Secured	Unsecured	Automobile	Total
V1	\$1,819,688	\$55,825,636	\$94,975,729	\$152,621,053
V2	—	35,100,419	910,517	36,010,936
V3	—	5,389,687	208,424	5,598,111
V4	—	4,773,597	163,498	4,937,095
V5	—	824,724	79,700	904,424
V6	—	470,151	12,847	482,998
V7	—	295,892	86,664	382,556
V8	—	323,147	45,105	368,252
V9	—	1,225,944	143,168	1,369,112
No risk grade	—	324,045	—	324,045
	\$1,819,688	\$104,553,242	\$96,625,652	\$202,998,582

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

Note 3 - Loans to Members (Continued)

Residential Real Estate Credit Quality

The Credit Union considers the performance of the residential real estate loan portfolio and its impact on the allowance for loan losses. Residential 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 recorded investment in residential real estate loans based on credit quality as of December 31, 2022 and 2021:

Risk Grade	2022			
	First Mortgage	Second Mortgage	HELOC	Total
V1	\$277,226,497	\$62,973,841	\$41,863,812	\$382,064,150
V2	1,597,722	295,373	460,192	2,353,287
V3	1,004,436	344,771	75,991	1,425,198
V4	—	175,537	256,537	432,074
V5	749,500	—	69,810	819,310
V6	—	—	354,448	354,448
V7	—	14,520	—	14,520
V8	389,047	7,852	13,907	410,806
V9	—	18,649	—	18,649
No risk grade	—	—	35,632	35,632
	\$280,967,202	\$63,830,543	\$43,130,329	\$387,928,074

Risk Grade	2021			
	First Mortgage	Second Mortgage	HELOC	Total
V1	\$196,689,958	\$29,020,758	\$27,134,412	\$252,845,128
V2	789,349	113,688	47,921	950,958
V3	3,051,355	25,041	19,224	3,095,620
V4	624,362	58,974	—	683,336
V5	1,313,519	16,720	—	1,330,239
V6	196,454	43,161	—	239,615
V7	—	—	—	—
V8	144,587	—	—	144,587
V9	—	—	—	—
No risk grade	761,256	—	36,032	797,288
	\$203,570,840	\$29,278,342	\$27,237,589	\$260,086,771

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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 recorded investment in commercial loans based on credit quality as of December 31, 2022 and 2021:

Risk Grade	2022			
	Agency Secured	Agency Unsecured	Real Estate	Total
V1	\$219,084,746	\$147,276,209	\$113,987,368	\$480,348,323
V2	3,384	37,881,028	74,365,191	112,249,603
V3	—	7,554,552	43,010,900	50,565,452
V4	—	2,838,275	27,619,395	30,457,670
V5	694	393,506	2,177,397	2,571,597
V6	—	352,972	—	352,972
V7	—	296,050	—	296,050
V8	—	106,784	—	106,784
V9	—	1,205,560	—	1,205,560
No risk grade	—	—	37,052	37,052
	\$219,088,824	\$197,904,936	\$261,197,303	\$678,191,063

Risk Grade	2021			
	Agency Secured	Agency Unsecured	Real Estate	Total
V1	\$214,361,427	\$131,149,149	\$94,795,720	\$440,306,296
V2	5,801	24,383,622	36,478,904	60,868,327
V3	1,984	3,706,709	24,918,010	28,626,703
V4	—	563,824	21,222,896	21,786,720
V5	—	850,225	2,726,953	3,577,178
V6	—	32,059	118,933	150,992
V7	—	4,990	—	4,990
V8	—	222,869	—	222,869
V9	—	1,105,216	1,556,552	2,661,768
No risk grade	—	—	—	—
	\$214,369,212	\$162,018,663	\$181,817,968	\$558,205,843

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

Note 4 - Property and Equipment

Property and equipment is carried at cost, less accumulated depreciation and amortization, and is summarized as of December 31, 2022 and 2021 by major classification as follows:

	2022	2021
Furniture and equipment	\$13,182,803	\$12,626,839
Leasehold improvements	3,648,497	3,648,497
	16,831,300	16,275,336
Less accumulated depreciation and amortization	(13,543,125)	(11,970,631)
	\$3,288,175	\$4,304,705

Depreciation and amortization charged to office operating costs was approximately \$1,580,000 and \$1,640,000 for the years ended December 31, 2022 and 2021, respectively.

Note 5 - Members' Shares and Savings Accounts

Members' shares and savings accounts are summarized as follows as of December 31, 2022 and 2021:

	2022	2021
Share accounts	\$350,032,079	\$279,844,234
Share draft accounts	223,073,297	229,189,919
Money market accounts	157,163,626	218,306,482
Individual retirement accounts (IRAs)	22,015,937	23,125,718
Share and IRA certificates	378,997,729	304,892,514
	\$1,131,282,668	\$1,055,358,867

As of December 31, 2022, scheduled maturities of share and IRA certificates are as follows:

	2022
Within one year	\$195,961,344
1 to 2 years	76,470,768
2 to 3 years	31,433,862
3 to 4 years	65,975,401
4 to 5 years	9,156,354
	\$378,997,729

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

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 \$153,837,000 as of December 31, 2022.

Included in share and IRA certificates above are non-member time deposits of approximately \$235,268,000 and \$205,706,000 as of December 31, 2022 and 2021, respectively.

Note 6 - Borrowed Funds

Lines of Credit

As of December 31, 2022 and 2021, 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 \$16,345,000 and \$18,000,000 as of December 31, 2022 and 2021, respectively.

As of December 31, 2022 and 2021, the Credit Union maintained an unused line of credit with Corporate One Federal Credit Union. 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 \$50,000,000 as of December 31, 2022 and 2021.

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 carrying amount of the pledged collateral was approximately \$81,922,000 and \$70,154,000 as of December 31, 2022 and 2021, respectively. Based on the collateral pledged, the maximum unused line of credit as of December 31, 2022 and 2021 was approximately \$58,098,000 and \$54,230,000, 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. The carrying amount of the pledged collateral was approximately \$497,609,000 and \$280,058,000 as of December 31, 2022 and 2021, respectively. Based on the collateral pledged, the maximum available line of credit as of December 31, 2022 and 2021 was approximately \$262,837,000 and \$166,459,000, respectively, of which approximately \$188,187,000 and \$71,510,000, respectively, was available.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

Note 6 - Borrowed Funds (Continued)

As of December 31, 2022 and 2021, the Credit Union had outstanding borrowings with the FHLB at interest rates ranging between 0.91% and 3.48%. All borrowings have a fixed rate of interest and the weighted average interest rates were 1.99% and 2.02% as of December 31, 2022 and 2021, respectively. The repayment schedule of the advances as of December 31, 2022 is as follows:

	<u>2022</u>
Within one year	\$13,800,000
1 to 2 years	8,200,000
2 to 3 years	42,700,000
3 to 4 years	—
4 to 5 years	4,100,000
Thereafter	5,850,000
	<u>\$74,650,000</u>

Note 7 - Employee Benefits

Retirement Plans

Credit Union management and staff are employed by the Credit Union's sponsor, Farmers, and leased back to the Credit Union. As such, Credit Union employees participate in Farmers' retirement plans and the Credit Union reimburses Farmers for the retirement plan expenses associated with the leased employees. As of January 1, 2019, the Credit Union implemented a matching 401(k) plan with an additional 4% base company contribution. The 401(k) matching plan through Farmers 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 and the 4% base company 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, 2022 and 2021 were approximately \$1,557,000 and \$1,391,000, respectively.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

Note 8 - Commitments and Contingent Liabilities

Lease Commitments

The Credit Union leases certain office facilities under long-term, non-cancellable operating leases that expire at various dates through 2032, some of which may include options to extend the leases for up to 11 years. Monthly payments range from \$2,000 to \$77,000, with certain leases requiring annual increases based on the Consumer Price Index and a monthly charge for common area maintenance based on actual costs incurred.

The total cost of operating leases, included in office occupancy expenses, was approximately \$1,433,000 and \$1,633,000 for the years ended December 31, 2022 and 2021, respectively.

Supplemental lease information is as follows for the year ended December 31, 2022:

	<u>2022</u>
Weighted-average remaining lease term	6.87 years
Weighted-average discount rate	1.75%
Cash paid for amounts included in measurement of lease liabilities:	
Operating cash flows from operating leases	\$1,065,226
Right-of-use assets obtained in exchange for operating lease liabilities	\$8,615,750

Remaining lease payments approximate the following as of December 31, 2022:

<u>Year ending December 31,</u>	<u>Amount</u>
2023	\$1,097,000
2024	1,129,000
2025	1,163,000
2026	1,198,000
2027	1,233,000
Thereafter	2,368,000
Total minimum lease payments	8,188,000
Less: imputed interest	(494,000)
Present value of lease liabilities	<u>\$7,694,000</u>

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.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

Note 8 - Commitments and Contingent Liabilities (Continued)

Off Balance-Sheet Risk (Continued)

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, 2022, the total unfunded commitments under such lines of credit was approximately \$272,009,000. 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 (PCA), 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.

Effective January 1, 2022, federally insured, natural-person credit unions defined as "complex" have to comply with the NCUA's risk-based capital ("RBC") final rule which amends NCUA's PCA regulations, part 702, or the newly created Complex Credit Union Leverage Ratio ("CCULR") rule. A credit union is defined as "complex" if the credit union's quarter-end total assets exceed \$500,000,000, as reflected in its most recent Call Report. The rules require credit unions taking certain risks to hold capital commensurate with those risks. The RBC rule revises part 702 of NCUA's current regulations to establish an RBC ratio measure that is the percentage of a credit union's capital divided by the credit union's defined risk weighted asset base. This RBC rule more closely aligns NCUA's risk weights with those assigned by other Banking agencies. Accordingly, the RBC rule adopts a 10 percent RBC ratio level for "well capitalized" credit unions, and an 8 percent RBC ratio level for "adequately capitalized" credit unions.

The CCULR rule simplifies the RBC rule requirements for complex credit unions that meet certain eligibility criteria by allowing them to choose between implementing the RBC rule or the CCULR. Credit unions that select CCULR instead of the RBC rule have a minimum 9 percent leverage ratio requirement. A qualifying complex credit union opting into the CCULR framework calculates its CCULR in the same manner as its net worth ratio under NCUA's PCA regulations, part 702. Management has opted into the CCULR framework as of December 31, 2022.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

Note 9 - Regulatory Capital (Continued)

As of December 31, 2022, the most recent call reporting period, the NCUA categorized the Credit Union as “*well capitalized*” under the CCULR regulatory framework for PCA. To be categorized as “*well capitalized*,” the Credit Union must maintain a minimum net worth ratio of 9.00% of assets. There are no conditions or events since that calculation 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:

	<u>As of December 31, 2022</u>	
	<u>Amount</u>	<u>Ratio/ Requirement</u>
Actual net worth	\$140,081,576	10.25%
Amount needed to be classified as “ <i>well capitalized</i> ”	\$123,032,828	9.00%

In performing its calculation of total assets as of December 31, 2022, the Credit Union used the quarter end option, as permitted by regulation.

Prior to January 1, 2022, credit unions were required to calculate a Risk-Based Net Worth Requirement (RBNWR) which established whether or not the Credit Union was considered “complex” under the regulatory framework. The Credit Union’s RBNWR as of December 31, 2021 was 6.30%. The minimum requirement to be considered complex under the regulatory framework was 6.00%.

The Credit Union’s actual net worth as of December 31, 2021 was \$132,127,265 with a net worth ratio of 10.21%. As of December 31, 2021, the NCUA categorized the Credit Union as “*well capitalized*” under the regulatory framework for PCA. To be categorized as “*well capitalized*” the Credit Union must maintain a minimum net worth ratio of 7.00% of assets.

Because the RBNWR was less than the net worth ratio as of December 31, 2021, the Credit Union retained its original category. Further, in performing its calculation of total assets as of December 31, 2021, the Credit Union used the quarter end option, as permitted by regulation.

Management believes, as of December 31, 2022 and 2021, that the Credit Union meets all capital adequacy requirements to which it is subject.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

Note 10 - Fair Value Measurement

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.

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, 2022			
	Level 1	Level 2	Level 3	Total
Available-for-sale debt securities:				
Mortgage-backed securities	\$—	\$306,423	\$—	\$306,423

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

NOTES TO THE FINANCIAL STATEMENTS DECEMBER 31, 2022 AND 2021

Note 10 - Fair Value Measurement

Assets Measured at Fair Value on a Recurring Basis (Continued)

	Assets at Fair Value as of December 31, 2021			
	Level 1	Level 2	Level 3	Total
Equity securities:				
Mutual funds	\$69,724,599	\$—	\$—	\$69,724,599
Available-for-sale debt securities:				
Mortgage-backed securities	—	393,731	—	393,731
Total	\$69,724,599	\$393,731	\$—	\$70,118,330

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 recorded investment 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, 2022			
	Level 1	Level 2	Level 3	Total
Impaired loans	\$—	\$—	\$4,724,143	\$4,724,143

	Assets at Fair Value as of December 31, 2021			
	Level 1	Level 2	Level 3	Total
Impaired loans	\$—	\$—	\$4,974,133	\$4,974,133

* * * End of Notes * * *