FARMERS INSURANCE
FEDERAL CREDIT UNION

BETTER **TOGETHER**

2019 Annual Report

2019 Highlights

Retained Earnings

2019	**$117,838,575**
2018	$110,377,176
2017	$104,392,126

Net Income

2019	**$7,461,399**
2018	$5,985,050
2017	$4,433,356

Total Net Loans

2019	**$843,165,649**
2018	$778,204,965
2017	$707,944,982

Membership Shares

2019	**$819,547,852**
2018	$707,213,059
2017	$640,675,567

Member Satisfaction Score

2019	**92.01%**
2018	93.06%
2017	90.33%

Total Assets

2019	**$1,004,416,958**
2018	$917,256,720
2017	$787,705,796

Total Members

2019	**55,018**
2018	52,865
2017	50,178

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

FINANCIAL STATEMENTS

DECEMBER 31, 2019 AND 2018
(With Independent Auditor's Report Thereon)

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

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Independent Auditor's Report

May 4, 2020

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, 2019 and 2018, 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.

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, 2019 and 2018, 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, 2019 AND 2018

Assets	**2019**	**2018**
Cash and cash equivalents	$22,250,759	$6,463,683
Interest bearing deposits	99,194,000	95,404,000
Investments:		
Available-for-sale	3,565,741	4,926,860
Credit Union Service Organizations	13,656,611	9,124,605
Federal Home Loan Bank (FHLB) stock	2,131,700	2,458,500
Loans to members, net of allowance for loan losses	843,165,649	778,204,965
Accrued interest receivable	4,123,496	3,755,952
Prepaid and other assets	5,046,723	5,723,787
Property and equipment	3,548,247	4,227,850
National Credit Union Share Insurance Fund (NCUSIF) deposit	7,734,032	6,966,518
Total assets	$1,004,416,958	$917,256,720
Liabilities and Members' Equity		
Liabilities:		
Members' shares and savings accounts	$819,547,852	$707,213,059
Borrowed funds	58,125,361	91,007,105
Accrued expenses and other liabilities	8,883,756	8,628,064
Total liabilities	886,556,969	806,848,228
Commitments and contingent liabilities		
Members' equity:		
Regular reserve	16,966,743	16,966,743
Undivided earnings	100,871,832	93,410,433
Accumulated other comprehensive income	21,414	31,316
Total members' equity	117,859,989	110,408,492
Total liabilities and members' equity	$1,004,416,958	$917,256,720

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF INCOME
YEARS ENDED DECEMBER 31, 2019 AND 2018

	2019	2018
Interest income:		
Loans to members	$52,192,753	$45,948,213
Investment securities	3,300,224	2,753,919
Total interest income	55,492,977	48,702,132
Interest expense:		
Members' shares and savings accounts	10,040,406	6,735,686
Borrowed funds	1,618,571	1,347,559
Total interest expense	11,658,977	8,083,245
Net interest income	43,834,000	40,618,887
Provision for loan losses	4,129,730	3,817,394
Net interest income after provision for loan losses	39,704,270	36,801,493
Non-interest income:		
Overdraft and share draft fees	3,232,928	3,483,400
Interchange income	3,055,178	3,092,196
Service charges and other fees	1,130,100	1,106,947
Other income	420,016	705,603
Total non-interest income	7,838,222	8,388,146
Non-interest expenses:		
Compensation and benefits	21,398,806	21,664,577
Office operating costs	8,176,090	7,804,469
Educational and promotional	3,460,493	3,320,507
Professional and outside services	1,974,907	1,757,360
Office occupancy	1,775,492	1,739,565
Other expenses	1,963,048	1,696,052
Loan servicing	1,332,257	1,222,059
Total non-interest expenses	40,081,093	39,204,589
Net income	$7,461,399	$5,985,050

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF COMPREHENSIVE INCOME
YEARS ENDED DECEMBER 31, 2019 AND 2018

	2019	2018
Net income	$7,461,399	$5,985,050
Other comprehensive loss:		
Available-for-sale investments:		
Net unrealized holding losses on available-for-sale investments	(9,902)	(12,716)
Reclassification adjustment for investment (gains)/losses included in net income	—	—
Other comprehensive loss	(9,902)	(12,716)
Comprehensive income	$7,451,497	$5,972,334

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF MEMBERS' EQUITY
YEARS ENDED DECEMBER 31, 2019 AND 2018

	Regular Reserve	Undivided Earnings	Accumulated Other Comprehensive Income/(Loss)	Total
Balance, December 31, 2017	$16,966,743	$87,425,383	$44,032	$104,436,158
Net income	—	5,985,050	—	5,985,050
Other comprehensive loss	—	—	(12,716)	(12,716)
Balance, December 31, 2018	16,966,743	93,410,433	31,316	110,408,492
Net income	—	7,461,399	—	7,461,399
Other comprehensive loss	—	—	(9,902)	(9,902)
Balance, December 31, 2019	$16,966,743	$100,871,832	$21,414	$117,859,989

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2019 AND 2018

	2019	2018
Cash flows from operating activities:		
Net income	$7,461,399	$5,985,050
Adjustments to net cash provided from operating activities:		
Provision for loan losses	4,129,730	3,817,394
Depreciation and amortization	1,384,227	1,354,906
Loss attributable to investments in Credit Union Service Organizations	467,994	287,834
Net changes in operating assets and liabilities:		
Increase in accrued interest receivable	(367,544)	(663,096)
Decrease/(increase) prepaid and other assets	677,064	(1,632,706)
Increase/(decrease) in accrued expenses and other liabilities	255,692	(1,041,399)
Total adjustments	6,547,163	2,122,933
Net cash provided from operating activities	14,008,562	8,107,983

See accompanying notes to the financial statements.

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION

STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2019 AND 2018

Cash Flows (Continued)

	2019	2018
Cash flows from investing activities:		
Proceeds from interest bearing deposits	112,664,000	97,949,000
Purchase of interest bearing deposits	(116,454,000)	(185,156,000)
Proceeds from maturities and repayments of available-for-sale investments	1,351,217	1,605,666
Proceeds from the maturity of held-to-maturity investments	—	3,120,000
Investment in Credit Union Service Organizations	(1,000,000)	(250,000)
Net change in loans to Credit Union Service Organizations	(4,000,000)	1,250,000
Redemption/(purchase) of FHLB stock	326,800	(732,500)
Net change in loans to members	(69,090,414)	(74,077,377)
Expenditures for property and equipment	(704,624)	(2,028,697)
Increase in NCUSIF deposit	(767,514)	(968,380)
Net cash used in investing activities	(77,674,535)	(159,288,288)
Cash flows from financing activities:		
Net change in members' shares and savings accounts	112,334,793	66,537,492
Proceeds from borrowed funds	7,700,000	58,650,000
Repayment of borrowed funds	(40,581,744)	(567,503)
Net cash provided from financing activities	79,453,049	124,619,989
Net change in cash and cash equivalents	15,787,076	(26,560,316)
Cash and cash equivalents - beginning	6,463,683	33,023,999
Cash and cash equivalents - ending	$22,250,759	$6,463,683

Supplemental Information

Interest paid	$11,658,977	$8,083,245

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 (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.

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.

Investments

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

Available-for-sale: Government and government agency mortgage-backed securities, guaranteed notes, and collateralized mortgage obligations 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 condition.

Held-to-Maturity: Negotiable certificates of deposit which the Credit Union has the positive intent and ability to hold to maturity are reported at cost, adjusted for amortization of premiums and accretion of discounts which are recognized in interest income over the period to maturity.

Unrealized gains and losses on available-for-sale investments are recognized as direct increases or decreases in other comprehensive income/(loss). Purchase premiums and discounts are recognized in interest income over the terms of the securities. Declines in the estimated fair value of available-for-sale 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) 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.

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, 2019 and 2018, 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, 2019, CMF's assets and liabilities approximated $11,617,000 and $5,914,000, respectively. As of December 31, 2018, CMF's assets and liabilities approximated $10,099,000 and $4,660,000, respectively. CMF reported net income/(loss) of approximately $337,000 and ($129,000) during the years ended December 31, 2019 and 2018, respectively. Additionally, the Credit Union has provided CMF a $5,000,000 line of credit to facilitate CMF's operations. The line of credit is secured by CMF's cash, receivables and intangible assets. The line of credit is variable rate and matures on May 31, 2021. As of December 31, 2019 and 2018, the outstanding balance of the line of credit was approximately $2,750,000 and $2,250,000, respectively.

As of December 31, 2019 and 2018, the Credit Union owned 20.3% of Extensia Financial, LLC (Extensia). Extensia provides business lending services (i.e. brokerage, servicing, consulting) to credit unions. As of December 31, 2019, Extensia's assets and liabilities approximated $19,899,000 and $14,886,000, respectively. As of December 31, 2018, Extensia's assets and liabilities approximated $15,984,000 and $10,494,000, respectively. Extensia reported net (loss)/income of approximately ($674,000) and $124,000 during the years ended December 31, 2019 and 2018, respectively. Additionally, the Credit Union has provided Extensia a $3,500,000 promissory note to facilitate Extensia's operations. The promissory note is secured by Extensia's cash, receivables and intangible assets. As of December 31, 2019 the outstanding balance of the promissory note was approximately $3,500,000.

As of December 31, 2019 and 2018, the Credit Union also owned 8.70% and 10.91%, 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, 2019, CDP's assets and liabilities approximated $26,159,000 and $1,723,000, respectively. As of December 31, 2018, CDP's assets and liabilities approximated $30,826,000 and $1,337,000, respectively. CDP reported net losses of approximately $5,053,000 and $2,432,000 during the years ended December 31, 2019 and 2018, respectively. 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.

During the year ended December 31, 2019, the Credit Union invested $1,000,000 in CU Railz, LLC (CU Railz). CU Railz offers an enhancement to the Credit Union's electronic bill pay platform and allows members to make payments to/from other financial institutions easily. The investment in CU Railz is accounted for under the cost method based on the Credit Union's percentage of ownership and/or level of influence exercised over the companies. Under the cost method, the investment is recorded at its historical cost unless there is evidence of impairment.

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

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.

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.

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

Allowance for Loan Losses (Continued)

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 determined 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.

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.

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

Allowance for Loan Losses (Continued)

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. 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. 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. 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.

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

Allowance for Loan Losses (Continued)

Residential Real Estate Segment Allowance Methodology (Continued)

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 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

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

Allowance for Loan Losses (Continued)

Impaired Loans (Continued)

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

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:

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

Allowance for Loan Losses (Continued)

Credit Quality Indicators (Continued)

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. 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.

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

Allowance for Loan Losses (Continued)

Credit Quality Indicators (Continued)

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.

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.

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

Allowance for Loan Losses (Continued)

Credit Quality Indicators (Continued)

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 - These loans are considered uncollectible and will be charged off immediately. 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.

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;

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

Allowance for Loan Losses (Continued)

Loan Charge-off Policies (Continued)

- 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.

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.

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.

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 within 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 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

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.

Overdraft and Share Draft Fees, Interchange Income and Service Charges and Other Fees

The Credit Union earns fee and commission income from a range of services it provides to its members. Deposit fee income and interchange fee income are earned on the execution of financial services performed. This includes fees arising from 1) services initiated or requested by the member, including overdrawn account charges, insufficient funds charges, and stop payment fees; 2) participating in transactions with members and third-party financial institutions, such as interchange fee income for authorizing and settling member debit and credit card point-of-sale or ATM transactions. Deposit fees and interchange revenue are presented as non-interest income in the consolidated statements of income, with related expense streams such as processor costs and reward point costs, presented separately in non-interest expenses.

Advertising Costs

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

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

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 Financial Accounting Standards Board (FASB) Accounting Standards Codification (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.

Recent Accounting Pronouncements

In June 2016, the FASB issued Accounting Standard 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 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 the Credit Union on January 1, 2023. 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 will be effective for the Credit Union on January 1, 2021 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 May 4, 2020, the date the financial statements were available to be issued. See Note 12.

Note 2 - Investments

The following table presents the amortized cost and estimated fair value of investments as of December 31, 2019:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
Mortgage-backed securities	$668,325	$21,808	($3)	$690,130
Collateralized mortgage obligations	2,876,002	—	(391)	2,875,611
	$3,544,327	$21,808	($394)	$3,565,741

The following table presents the amortized cost and estimated fair value of investments as of December 31, 2018:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
Mortgage-backed securities	$844,028	$25,508	($39)	$869,497
Collateralized mortgage obligations	4.051,516	5,847	—	4,057,363
	$4,895,544	$31,355	($39)	$4,926,860

As of December 31, 2019, 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 one to eight 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.

Note 2 - Investments (Continued)

Information pertaining to investments with gross unrealized losses as of December 31, 2019, 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:						
Mortgage-backed securities	$5,131	($3)	$—	$—	$5,131	($3)
Collateralized mortgage obligations	2,875,611	(391)	—	—	2,875,611	(391)
	$3,690,742	($394)	$—	$—	$3,690,742	($394)

Information pertaining to investments with gross unrealized losses as of December 31, 2018, 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:						
Mortgage-backed securities	$16,393	($39)	$—	$—	$16,393	($39)

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.

Note 3 - Loans to Members

The composition of loans to members as of December 31, 2019 and 2018 is as follows:

	2019	2018
Consumer:		
Unsecured	$89,792,872	$89,228,710
Automobile	95,426,417	99,955,390
Other secured	1,936,821	1,711,502
	187,156,110	190,895,602
Residential Real Estate:		
First mortgage	101,405,729	94,056,368
Second mortgage	29,034,438	22,014,989
HELOC	26,381,582	25,678,754
	156,821,749	141,750,111
Commercial:		
Agency secured	233,808,441	224,363,191
Agency unsecured	103,692,111	72,728,000
Real estate	168,557,723	155,774,553
	506,058,275	452,865,744
Total loans	850,036,134	785,511,457
Deferred loan origination fees/costs, net	(728,721)	(1,271,925)
	849,307,413	784,239,532
Less: Allowance for loan losses	(6,141,764)	(6,034,567)
Loans to members, net	$843,165,649	$778,204,965

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, 2019:

	Consumer	Residential Real Estate	Commercial	Total
Allowance for loan losses:				
Beginning allowance	$3,346,513	$945,391	$1,742,663	$6,034,567
Charge-offs	(3,952,864)	(17,437)	(991,239)	(4,961,540)
Recoveries	781,862	63,960	93,185	939,007
Provision for loan losses	3,290,380	(45,723)	885,073	4,129,730
Ending allowance	$3,465,891	$946,191	$1,729,682	$6,141,764
Ending balance individually evaluated for impairment	$8,274	$792,812	$—	$801,086
Ending balance collectively evaluated for impairment	3,457,617	153,379	1,729,682	5,340,678
Ending allowance	$3,465,891	$946,191	$1,729,682	$6,141,764

The following table presents a summary of the recorded investment in loans by portfolio segment as of December 31, 2019:

	Consumer	Residential Real Estate	Commercial	Total
Loans:				
Ending balance individually evaluated for impairment	$271,398	$6,520,687	$—	$6,792,085
Ending balance collectively evaluated for impairment	186,886,557	150,425,326	505,203,445	842,515,328
Total loans	$187,157,955	$156,946,013	$505,203,445	$849,307,413

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, 2018:

	Consumer	Residential Real Estate	Commercial	Total
Allowance for loan losses:				
Beginning allowance	$3,356,602	$1,162,761	$1,435,129	$5,954,492
Charge-offs	(3,740,669)	(129,987)	(941,122)	(4,811,778)
Recoveries	781,436	234,499	58,524	1,074,459
Provision for loan losses	2,949,144	(321,882)	1,190,132	3,817,394
Ending allowance	$3,346,513	$945,391	$1,742,663	$6,034,567
Ending balance individually evaluated for impairment	$8,385	$889,133	$—	$897,518
Ending balance collectively evaluated for impairment	3,338,128	56,258	1,742,663	5,137,049
Ending allowance	$3,346,513	$945,391	$1,742,663	$6,034,567

The following table presents a summary of the recorded investment in loans by portfolio segment as of December 31, 2018:

	Consumer	Residential Real Estate	Commercial	Total
Loans:				
Ending balance individually evaluated for impairment	$227,378	$8,018,794	$—	$8,246,172
Ending balance collectively evaluated for impairment	190,677,767	133,832,358	451,483,235	775,993,360
Total loans	$190,905,145	$141,851,152	$451,483,235	$784,239,532

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, 2019:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With an allowance recorded:					
Consumer:					
Unsecured	$245,035	$245,037	$8,192	$216,048	$23,295
Automobile	$26,363	$26,363	$82	$33,341	$1,333
Residential Real Estate:					
First mortgage	$6,088,970	$6,081,183	$789,226	$6,768,113	$545,587
Second mortgage	$306,010	$306,010	$3,583	$229,418	$12,809
HELOC	$125,707	$125,746	$3	$272,210	$19,591
Totals by loan segment:					
Consumer	$271,398	$271,400	$8,274	$249,389	$24,628
Residential Real Estate	6,520,687	6,512,939	792,812	7,269,741	577,987
Total	$6,792,085	$6,784,339	$801,086	$7,519,130	$602,615

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, 2018:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With an allowance recorded:					
Consumer:					
Unsecured	$187,060	$187,060	$7,908	$141,746	$14,827
Automobile	$40,318	$40,318	$477	$41,395	$1,135
Residential Real Estate:					
First mortgage	$7,447,255	$7,438,619	$889,126	$6,985,340	$328,075
Second mortgage	$152,826	$152,826	$3	$262,261	$13,928
HELOC	$418,713	$418,808	$4	$442,897	$44,175
Totals by loan segment:					
Consumer	$227,378	$227,378	$8,385	$183,141	$15,962
Residential Real Estate	8,018,794	8,010,253	889,133	7,690,498	386,178
Total	$8,246,172	$8,237,631	$897,518	$7,873,639	$402,140

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, 2019:

	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Current	Total loans
Consumer:						
Unsecured	$1,064,051	$442,724	$1,109,406	$2,616,181	$87,178,536	$89,794,717
Automobile	544,904	161,063	524,286	1,230,253	94,196,164	95,426,417
Other secured	1,150	—	2,351	3,501	1,933,320	1,936,821
Total	1,610,105	603,787	1,636,043	3,849,935	183,308,020	187,157,955
Residential Real Estate:						
First mortgage	1,067,456	—	1,560,985	2,628,441	98,909,990	101,538,431
Second mortgage	132,728	271,080	34,930	438,738	28,595,700	29,034,438
HELOC	182,588	49,445	76,262	308,295	26,064,849	26,373,144
Total	1,382,772	320,525	1,672,177	3,375,474	153,570,539	156,946,013
Commercial:						
Agency secured	136,544	143,706	114,242	394,492	233,413,949	233,808,441
Agency unsecured	80,626	265,450	144,792	490,868	103,201,243	103,692,111
Real estate	—	—	—	—	167,702,893	167,702,893
Total	217,170	409,156	259,034	885,360	504,318,085	505,203,445
Grand Total	$3,210,047	$1,333,468	$3,567,254	$8,110,769	$841,196,644	$849,307,413

Loans on which the accrual of interest has been discontinued or reduced approximated $3,567,000 as of December 31, 2019. There were no loans 90 days or more past due and still accruing interest as of December 31, 2019.

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, 2018:

	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Current	Total Loans
Consumer:						
Unsecured	$1,165,974	$481,939	$912,095	$2,560,008	$86,678,245	$89,238,253
Automobile	718,715	133,940	393,048	1,245,253	98,710,137	99,955,390
Other secured	—	—	—	—	1,711,502	1,711,502
Total	1,884,689	615,879	1,305,143	3,805,261	187,099,884	190,905,145
Residential Real Estate:						
First mortgage	1,546,939	2,290,915	718,057	4,555,911	89,607,294	94,163,205
Second mortgage	128,402	40,842	111,984	281,228	21,733,761	22,014,989
HELOC	150,058	276,630	142,083	568,771	25,104,187	25,672,958
Total	1,825,399	2,608,387	972,124	5,405,910	136,445,242	141,851,152
Commercial:						
Agency secured	146,043	126,902	123,409	396,354	223,966,837	224,363,191
Agency unsecured	241,916	107,096	158,750	507,762	72,220,238	72,728,000
Real estate	193,023	—	—	193,023	154,199,021	154,392,044
Total	580,982	233,998	282,159	1,097,139	450,386,096	451,483,235
Grand Total	$4,291,070	$3,458,264	$2,559,426	$10,308,310	$773,931,222	$784,239,532

Loans on which the accrual of interest has been discontinued or reduced approximated $2,559,000 as of December 31, 2018. There were no loans 90 days or more past due and still accruing interest as of December 31, 2018.

Note 3 - Loans to Members (Continued)

Troubled Debt Restructurings

The income statement impact of approved TDRs was immaterial for financial statement disclosure for the years ended December 31, 2019 and 2018. 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, 2019:

	Number of Contracts	Recorded Investment in TDRs Approved	TDRs Which Subsequently Defaulted
Consumer:			
Unsecured	9	$193,618	$90,746

The following table presents TDR activity by class of loans as of December 31, 2018:

	Number of Contracts	Recorded Investment in TDRs Approved	TDRs Which Subsequently Defaulted
Consumer:			
Unsecured	12	$132,838	$—
Automobile	1	25,843	—
Total	13	$158,681	$—

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, 2019 and 2018:

	2019			
Risk Grade	**Other secured**	**Unsecured**	**Automobile**	**Total**
V1	$—	$56,477,311	$91,996,462	$148,473,773
V2	—	14,965,154	1,512,123	16,477,277
V3	—	8,251,602	756,130	9,007,732
V4	—	4,733,142	316,011	5,049,153
V5	—	1,465,751	102,123	1,567,874
V6	—	577,888	101,567	679,455
V7	—	506,789	110,544	617,333
V8	—	485,169	112,245	597,414
V9	—	1,818,805	419,212	2,238,017
No risk grade	1,936,821	513,106	—	2,449,927
	$1,936,821	$89,794,717	$95,426,417	$187,157,955

	2018			
Risk Grade	**Other secured**	**Unsecured**	**Automobile**	**Total**
V1	$—	$50,571,300	$96,895,905	$147,467,205
V2	—	20,585,499	1,517,159	22,102,658
V3	—	8,058,289	470,450	8,528,739
V4	—	4,559,601	452,843	5,012,444
V5	—	2,006,824	171,726	2,178,550
V6	—	849,756	48,576	898,332
V7	—	580,552	96,792	677,344
V8	—	229,449	65,408	294,857
V9	—	1,218,939	236,531	1,455,470
No risk grade	1,711,502	578,044	—	2,289,546
	$1,711,502	$89,238,253	$99,955,390	$190,905,145

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, 2019 and 2018:

	2019			
Risk Grade	**First**	**Second**	**HELOC**	**Total**
V1	$97,552,324	$26,025,717	$25,306,634	$148,884,675
V2	1,346,794	1,629,136	302,833	3,278,763
V3	134,430	459,040	407,609	1,001,079
V4	1,131,721	483,406	49,906	1,665,033
V5	534,105	197,612	80,098	811,815
V6	282,327	—	186,303	468,630
V7	—	112,632	—	112,632
V8	—	—	—	—
V9	—	126,895	39,761	166,656
No risk grade	556,730	—	—	556,730
	$101,538,431	$29,034,438	$26,373,144	$156,946,013

	2018			
Risk Grade	**First**	**Second**	**HELOC**	**Total**
V1	$88,376,456	$21,524,702	$25,031,472	$134,932,630
V2	1,796,318	130,171	146,584	2,073,073
V3	673,023	82,749	50,601	806,373
V4	573,367	115,372	25,588	714,327
V5	—	37,454	260,301	297,755
V6	86,264	88,106	16,329	190,699
V7	—	36,435	142,083	178,518
V8	—	—	—	—
V9	—	—	—	—
No risk grade	2,657,777	—	—	2,657,777
	$94,163,205	$22,014,989	$25,672,958	$141,851,152

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, 2019 and 2018:

	2019			
Risk Grade	**Agency**	**Agency**	**Real Estate**	**Total**
V1	$—	$65,010,885	$153,542,265	$218,553,150
V2	—	25,272,077	2,782,652	28,054,729
V3	—	7,403,596	4,707,136	12,110,732
V4	—	3,597,466	4,201,140	7,798,606
V5	—	1,348,109	—	1,348,109
V6	—	545,900	—	545,900
V7	—	88,823	—	88,823
V8	—	—	—	—
V9	—	425,255	—	425,255
No risk grade	233,808,441	—	2,469,700	236,278,141
	$233,808,441	$103,692,111	$167,702,893	$505,203,445

	2018			
Risk Grade	**Agency**	**Agency**	**Real Estate**	**Total**
V1	$—	$46,518,558	$88,086,915	$134,605,473
V2	—	15,145,096	50,612,113	65,757,209
V3	—	6,285,105	10,950,272	17,235,377
V4	—	3,216,536	4,742,744	7,959,280
V5	—	676,079	—	676,079
V6	—	316,310	—	316,310
V7	—	340,327	—	340,327
V8	—	—	—	—
V9	—	229,989	—	229,989
No risk grade	224,363,191	—	—	224,363,191
	$224,363,191	$72,728,000	$154,392,044	$451,483,235

Note 4 - Property and Equipment

Property and equipment is carried at cost, less accumulated depreciation and amortization, and is summarized as of December 31, 2019 and 2018 by major classification as follows:

	2019	**2018**
Furniture and equipment	$15,605,402	$15,249,011
Leasehold improvements	2,878,077	2,890,826
	18,483,479	18,139,837
Less accumulated depreciation and amortization	(14,935,232)	(13,911,987)
	$3,548,247	$4,227,850

Depreciation and amortization charged to office operating costs was approximately $1,384,000 and $1,355,000 for the years ended December 31, 2019 and 2018, respectively.

Note 5 - Members' Shares and Savings Accounts

Members' shares and savings accounts are summarized as follows as of December 31, 2019 and 2018:

	2019	**2018**
Share accounts	$152,756,057	$139,209,207
Share draft accounts	146,801,093	136,392,273
Money market accounts	178,154,927	198,529,725
Individual retirement accounts	24,633,622	27,565,121
Share and IRA certificates	317,202,153	205,516,733
	$819,547,852	$707,213,059

As of December 31, 2019, scheduled maturities of share and IRA certificates are as follows:

	2019
Within one year	$159,319,648
1 to 2 years	104,874,451
2 to 3 years	27,658,964
3 to 4 years	18,477,896
4 to 5 years	6,871,194
	$317,202,153

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 $46,400,000 as of December 31, 2019.

Included in share and IRA certificates above are non-member time deposits of approximately $211,142,000 and $99,715,000 as of December 31, 2019 and 2018, respectively.

Note 6 - Borrowed Funds

Lines of Credit

As of December 31, 2019 and 2018, 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 as of December 31, 2019 and 2018.

As of December 31, 2019 and 2018, 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 $10,000,000 as of December 31, 2019 and 2018.

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 $84,599,000 and $84,842,000 as of December 31, 2019 and 2018, respectively. Based on the collateral pledged, the maximum unused line of credit as of December 31, 2019 and 2018 was approximately $66,015,000 and $63,143,000, 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 $190,414,000 and $209,358,000 as of December 31, 2019 and 2018, respectively. Based on the collateral pledged, the maximum available line of credit as of December 31, 2019 and 2018 was approximately $121,593,000 and $130,628,000, respectively, of which approximately $63,468,000 and $39,621,000, respectively, was available.

Note 6 - Borrowed Funds (Continued)

The advances outstanding are as follows as of December 31, 2019 and 2018:

Lender	Interest Type	Interest Rate	Final Maturity Date	Payment Type	2019	2018
FHLB	Fixed	2.57%	March 6, 2019	Interest Only	$—	$40,000,000
FHLB	Fixed	1.45%	August 11, 2021	Amortizing	4,965,229	5,158,890
FHLB	Fixed	2.20%	March 29, 2022	Amortizing	12,460,132	12,848,215
FHLB	Fixed	1.99%	August 18, 2022	Interest Only	3,150,000	3,150,000
FHLB	Fixed	2.14%	September 29, 2022	Interest Only	5,500,000	5,500,000
FHLB	Fixed	2.99%	September 6, 2023	Interest Only	5,000,000	5,000,000
FHLB	Fixed	3.20%	September 25, 2023	Interest Only	5,400,000	5,400,000
FHLB	Fixed	3.23%	September 25, 2023	Interest Only	2,200,000	2,200,000
FHLB	Fixed	3.14%	November 30, 2023	Interest Only	1,200,000	1,200,000
FHLB	Fixed	2.45%	September 30, 2024	Interest Only	3,600,000	3,600,000
FHLB	Fixed	3.41%	September 24, 2025	Interest Only	2,100,000	2,100,000
FHLB	Fixed	2.83%	September 29, 2027	Interest Only	2,100,000	2,100,000
FHLB	Fixed	3.40%	July 17, 2028	Interest Only	1,250,000	1,250,000
FHLB	Fixed	3.48%	September 14, 2028	Interest Only	1,500,000	1,500,000
FHLB	Fixed	2.48%	April 10, 2024	Interest Only	4,600,000	—
FHLB	Fixed	2.88%	March 28, 2029	Interest Only	3,100,000	—
					$58,125,361	$91,007,105

The outstanding balances by maturity as of December 31, 2019 are as follows:

	2019
Within one year	$—
1 to 2 years	4,965,229
2 to 3 years	21,110,132
3 to 4 years	13,800,000
4 to 5 years	6,700,000
Thereafter	11,550,000
	$58,125,361

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 December 31, 2019, the retirement plans for pension and the Cash Balance Program were frozen, and a matching 401(k) plan with an additional 4% base company contribution was implemented on January 1, 2019. 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, 2019 and 2018 were approximately $1,306,000 and $1,818,000, 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, 2019:

Year ending December 31,	Amount
2020	$1,181,000
2021	1,326,000
2022	1,348,000
2023	1,274,000
2024	1,215,000
Thereafter	6,063,000
	$12,407,000

Net rent expense under operating leases, included in office occupancy expenses, was approximately $1,370,000 and $1,391,000 for the years ended December 31, 2019 and 2018, 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, 2019, the total unfunded commitments under such lines of credit was approximately \$199,810,000. 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, 2019 and 2018 was 6.40% and 6.16%, respectively. The minimum requirement to be considered complex under the regulatory framework is 6.00%. Management believes, as of December 31, 2019 and 2018, that the Credit Union meets all capital adequacy requirements to which it is subject.

Note 9 - Regulatory Capital (Continued)

As of December 31, 2019, 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, 2019		As of December 31, 2018	
	Amount	Ratio/ Requirement	Amount	Ratio/ Requirement
Actual net worth	$117,838,575	11.73%	$110,377,176	12.03%
Amount needed to meet the minimum RBNW requirement	$64,282,685	6.40%	$56,503,014	6.16%
Amount needed to be classified as "well capitalized"	$70,309,187	7.00%	$64,207,970	7.00%
Amount needed to be classified as "adequately capitalized"	$60,265,017	6.00%	$55,035,403	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 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.

Note 10 - Fair Value Measurement (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, 2019			
	Level 1	**Level 2**	**Level 3**	**Total**
Available-for-sale:				
Mortgage-backed securities	$—	$690,130	$—	$690,130
Collateralized mortgage obligations	—	2,875,611	—	2,875,611
	$—	$3,565,741	$—	$3,565,741

	Assets at Fair Value as of December 31, 2018			
	Level 1	**Level 2**	**Level 3**	**Total**
Available-for-sale:				
Mortgage-backed securities	$—	$869,497	$—	$869,497
Collateralized mortgage obligations	—	4,057,363	—	4,057,363
	$—	$4,926,860	$—	$4,926,860

Note 10 - Fair Value Measurement (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 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, 2019			
	Level 1	**Level 2**	**Level 3**	**Total**
Impaired loans	$—	$—	$5,990,999	$5,990,999

	Assets at Fair Value as of December 31, 2018			
	Level 1	**Level 2**	**Level 3**	**Total**
Impaired loans	$—	$—	$7,348,654	$7,348,654

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 were approximately $586,000 and $1,248,000 as of December 31, 2019 and 2018, respectively.

Deposits

Deposits of Credit Union directors and executive officers were approximately $2,198,000 and $2,266,000 as of December 31, 2019 and 2018, respectively.

Note 12 - Subsequent Event

Global efforts to contain the spread of COVID-19, often referred to as the Coronavirus, have significantly impacted many businesses and the economy. While the situation is evolving rapidly, and the full impact is not yet known, the disruption caused by the Coronavirus is affecting business and consumer activities worldwide–including disruption to major financial markets, supply chains, interruption of production, limited personnel, facility and store closures, and decreased demand from both business customers and consumers.

On April 7, 2020, the federal and state financial institution regulators (collectively the Agencies) issued a revised Interagency Statement on Loan Modifications and Reporting for Financial Institutions Working with Customers Affected by the Coronavirus (the Statement). The Statement includes guidance on TDRs, accounting for loan modifications, past due reporting, non-accrual loans and charge-offs among other items. A significant aspect of this Statement is the concept that the Agencies will not automatically categorize all COVID-19 related loan modifications as TDRs. The Agencies have confirmed with staff of the FASB that short-term modifications made on a good faith basis in response to COVID-19 to borrowers who were current prior to any relief, are not TDRs. This includes short-term (e.g., six months) modifications such as payment deferrals, fee waivers, extensions of repayment terms, or other delays in payment that are insignificant. Borrowers considered current are those that are less than 30 days past due on December 31, 2019. The Agencies' examiners will exercise judgment in reviewing loan modifications, including TDRs, and will not automatically adversely risk rate credits that are affected by COVID-19, including those considered TDRs.

With regard to the loans not otherwise reportable as past due, financial institutions are not expected to designate loans with deferrals granted due to COVID-19 as past due because of the deferral. If a financial institution agrees to a payment deferral, this may result in no contractual payments being past due, and these loans are not considered past due during the period of the deferral.

The Credit Union will determine if loans to stressed borrowers should be reported as nonaccrual assets in regulatory reports. However, during the short-term arrangements discussed in this statement, these loans generally may not be reported as nonaccrual.

As of May 4, 2020, the Credit Union is assessing the impact on its operations, but currently the ultimate effects of COVID-19 are unknown.

* * * End of Notes * * *