

**SAFE CREDIT UNION**  
Folsom, California

**FINANCIAL STATEMENTS**  
December 31, 2015 and 2014

**SAFE CREDIT UNION**

Folsom, California

**FINANCIAL STATEMENTS**

December 31, 2015 and 2014

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## INDEPENDENT AUDITOR'S REPORT

Supervisory Committee  
SAFE Credit Union  
Folsom, California

**Report on the Financial Statements**

We have audited the accompanying financial statements of SAFE Credit Union, which comprise the statements of financial condition as of December 31, 2015 and 2014, and the related statements of net income and 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 audit 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 SAFE Credit Union as of December 31, 2015 and 2014, 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.



Crowe Horwath LLP

Sacramento, California  
February 26, 2016

**SAFE CREDIT UNION**  
**STATEMENTS OF FINANCIAL CONDITION**  
**December 31, 2015 and 2014**  
(Dollar amounts in thousands)

	<u>2015</u>	<u>2014</u>
<b>ASSETS</b>		
Cash and cash equivalents	\$ 149,831	\$ 180,266
Investments:		
Available-for-sale	492,851	512,469
Other	9,740	9,740
Loans held for sale	5,559	1,618
Loans, net of allowance \$16,162 and \$16,820 as of December 31, 2015 and 2014, respectively	1,432,194	1,243,501
Accrued interest receivable	5,577	5,874
Property and equipment, net	54,618	54,051
Share insurance deposits	19,470	18,654
Goodwill	13,282	13,282
Other intangible assets	196	-
Other assets	<u>98,774</u>	<u>98,179</u>
 Total assets	 \$ <u>2,282,092</u>	 \$ <u>2,137,634</u>
 <b>LIABILITIES AND MEMBERS' EQUITY</b>		
Liabilities		
Members' shares	\$ 2,024,072	\$ 1,908,334
Public unit shares	25,004	5,001
Accrued expenses and other liabilities	<u>15,756</u>	<u>14,567</u>
 Total liabilities	 <u>2,064,832</u>	 <u>1,927,902</u>
 Commitments and contingent liabilities (Note 10)		
Members' equity		
Retained earnings, restricted	216,985	207,581
Accumulated other comprehensive income	<u>275</u>	<u>2,151</u>
 Total members' equity	 <u>217,260</u>	 <u>209,732</u>
 Total liabilities and members' equity	 \$ <u>2,282,092</u>	 \$ <u>2,137,634</u>

See accompanying notes.

**SAFE CREDIT UNION**  
**STATEMENTS OF NET INCOME AND COMPREHENSIVE INCOME**  
**For the Years Ended December 31, 2015 and 2014**  
(Dollar amounts in thousands)

	<u>2015</u>	<u>2014</u>
Interest income:		
Interest on loans	\$ 51,625	\$ 48,815
Interest on investments and cash equivalents	<u>9,518</u>	<u>9,857</u>
	<u>61,143</u>	<u>58,672</u>
Interest expense:		
Dividends on members' and public unit shares	6,083	6,174
Interest expense on borrowed and escrowed funds	<u>146</u>	<u>86</u>
	<u>6,229</u>	<u>6,260</u>
Net interest income	54,914	52,412
Provision for loan losses	<u>4,297</u>	<u>5,125</u>
Net interest income after provision for loan losses	<u>50,617</u>	<u>47,287</u>
Noninterest income:		
ATM and debit card fees	15,197	13,403
Account service fees	12,161	12,233
Loan fees	4,553	3,307
Securities and insurance fees	3,348	2,998
Gain on sale of loans	3,611	2,580
Other noninterest income	<u>3,337</u>	<u>3,000</u>
Total noninterest income	<u>42,207</u>	<u>37,521</u>
General and administrative expenses:		
Salaries and benefits	46,332	40,742
Office occupancy and operations	13,396	12,657
Professional services	13,180	12,034
Other	<u>10,512</u>	<u>9,006</u>
Total general and administrative expenses	<u>83,420</u>	<u>74,439</u>
Net income	<u>9,404</u>	<u>10,369</u>
Other comprehensive income:		
Unrealized (loss) gain on investments available-for-sale	<u>(1,876)</u>	<u>2,063</u>
Total other comprehensive (loss) income	<u>(1,876)</u>	<u>2,063</u>
Comprehensive income	<u>\$ 7,528</u>	<u>\$ 12,432</u>

See accompanying notes.

**SAFE CREDIT UNION**  
**STATEMENTS OF MEMBERS' EQUITY**  
**For the Years Ended December 31, 2015 and 2014**  
(Dollar amounts in thousands)

	Retained Earnings				Accumulated Other Comprehensive Income (Loss)	Total
	Regular Reserve	Other Appropriated	Unappropriated	Total		
Balance, December 31, 2013	\$ 38,700	\$ 158,512	\$ -	\$ 197,212	\$ 88	\$ 197,300
Net income	-	-	10,369	10,369	-	10,369
Net change in unrealized gain on available-for-sale investments	-	-	-	-	2,063	2,063
Appropriations	-	10,369	(10,369)	-	-	-
Balance, December 31, 2014	\$ 38,700	\$ 168,881	\$ -	\$ 207,581	\$ 2,151	\$ 209,732
Net income	-	-	9,404	9,404	-	9,404
Net change in unrealized gain on available-for-sale investments	-	-	-	-	(1,876)	(1,876)
Appropriations	-	9,404	(9,404)	-	-	-
Balance, December 31, 2015	<u>\$ 38,700</u>	<u>\$ 178,285</u>	<u>\$ -</u>	<u>\$ 216,985</u>	<u>\$ 275</u>	<u>\$ 217,260</u>

See accompanying notes.

**SAFE CREDIT UNION**  
**STATEMENTS OF CASH FLOWS**  
**For the Years Ended December 31, 2015 and 2014**  
(Dollar amounts in thousands)

	<u>2015</u>	<u>2014</u>
Cash Flows from Operating Activities		
Net income	\$ 9,404	\$ 10,369
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of servicing rights	672	575
Amortization of investment premiums, net	4,774	5,908
Provision for loan losses	4,297	5,125
Depreciation and amortization	4,228	3,286
Net loss on disposition of property and equipment	74	563
Net loss on disposition of other assets	240	-
Net (gain) loss on sale of other real estate owned	(861)	15
Net gain on sale of loans	(3,611)	(2,580)
Originations of loans held for sale	(135,337)	(87,863)
Proceeds from sale of loans held for sale	135,007	98,802
Net change in:		
Cash surrender value of company-owned life insurance policies	512	(821)
Accrued interest receivable	297	377
Other assets	17,570	(22,326)
Accrued expenses and other liabilities	<u>1,189</u>	<u>1,075</u>
<b>Net cash provided by operating activities</b>	<b><u>38,455</u></b>	<b><u>12,505</u></b>
Cash Flows from Investing Activities		
Purchases of available-for-sale investments	(114,113)	(55,005)
Proceeds from maturities of available-for-sale investments	127,081	97,754
Net change in other investments	-	(208)
Net change in loans	(194,410)	(158,651)
Net change in share insurance deposits	(816)	(1,141)
Proceeds from sale of other real estate owned	2,692	1,006
Purchases of property and equipment	(4,869)	(8,782)
Proceeds from sale of property and equipment	-	2,511
Purchases of intangible assets	(196)	-
Purchases of company-owned life insurance policies	<u>(20,000)</u>	<u>-</u>
<b>Net cash used in investing activities</b>	<b><u>(204,631)</u></b>	<b><u>(122,516)</u></b>
Cash Flows from Financing Activities		
Net increase in members' shares	115,738	119,423
Net increase in public unit shares	<u>20,003</u>	<u>-</u>
<b>Net cash provided by financing activities</b>	<b><u>135,741</u></b>	<b><u>119,423</u></b>
<b>(Decrease) increase in cash and cash equivalents</b>	<b>(30,435)</b>	<b>9,412</b>
Cash and cash equivalents, beginning of year	<u>180,266</u>	<u>170,854</u>
Cash and cash equivalents, end of year	<b><u>\$ 149,831</u></b>	<b><u>\$ 180,266</u></b>

See accompanying notes.

**SAFE CREDIT UNION**  
**STATEMENTS OF CASH FLOWS**  
**For the Years Ended December 31, 2015 and 2014**  
(Dollar amounts in thousands)

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	<u>2015</u>	<u>2014</u>
Supplemental Disclosures of Cash Flow Information		
Dividends paid on members' and public unit shares and interest paid on borrowed and escrowed funds	<u>\$ 6,229</u>	<u>\$ 6,260</u>
Loans transferred to other real estate owned	<u>\$ 1,420</u>	<u>\$ 3,942</u>

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See accompanying notes.



**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES AND NATURE OF OPERATIONS**

Nature of operations: SAFE Credit Union (the Credit Union) is a state-chartered credit union organized under the provisions of the California Credit Union Act. Participation in the Credit Union is limited to those individuals who qualify for membership which is defined in the Credit Union's Charter and Bylaws.

The Credit Union provides financial services through its branches in Sacramento and the surrounding counties. Its primary member share products are checking, savings, and term certificate accounts, and its primary lending products are residential real estate, vehicle, and commercial loans. Substantially all loans are secured by specific items of collateral including business assets, consumer assets, and commercial and residential real estate. Commercial loans are expected to be repaid from cash flow from operations of businesses. There are no significant concentrations of loans to any one industry or member. However, the members' ability to repay their loans is dependent on the real estate and general economic conditions in the area.

Significant accounting policies: The Credit Union follows the accounting standards set by the Financial Accounting Standards Board (FASB). The FASB establishes generally accepted accounting principles (GAAP) that are followed to ensure consistent reporting of the financial condition, results of operations and cash flows of the Credit Union. References to GAAP issued by the FASB in these notes are to the *FASB Accounting Standards Codification<sup>TM</sup>*, commonly referred to as the Codification or ASC.

Use of estimates: To prepare financial statements in conformity with accounting principles generally accepted in the United States of America management makes estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the financial statements and the disclosures provided and actual results could differ.

Subsequent events: The Credit Union has evaluated subsequent events for recognition and disclosure through February 26, 2016, the date on which the financial statements were available to be issued.

Concentrations of credit risk: Most of the Credit Union's business activity is with its members, many of whom live, work or worship in the following counties: Amador, Butte, Contra Costa, El Dorado, Nevada, Placer, Sacramento, San Joaquin, Solano, Sutter, Yolo and Yuba. The Credit Union may be exposed to credit risk resulting from these geographic concentrations. Although the Credit Union has a diversified loan portfolio, borrowers' ability to repay loans may be affected by the economic climate of the geographic regions in which borrowers reside. Management continually monitors the Credit Union's operations, including the loan portfolio, for potential impairment and other accounting consequences associated with concentration risk.

Fair value: The Codification defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. Fair value is a market-based measurement, not an entity-specific measurement, and the hierarchy gives the highest priority to quoted prices in active markets. Fair value measurements are disclosed by level within the fair value hierarchy.

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES AND NATURE OF OPERATIONS (Continued)**

Cash and cash equivalents: For the purpose of the statements of financial condition and cash flows, cash and cash equivalents include cash on hand, amounts due from financial institutions, and highly liquid debt instruments classified as cash that were purchased with maturities of three months or less. Amounts due from financial institutions may, at times, exceed federally insured limits.

Investments: Debt securities that management has the positive intent and ability to hold to maturity are classified as held-to-maturity and recorded at amortized cost. Securities not classified as held-to-maturity are classified as available-for-sale and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income.

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method. Declines in the fair value of individual available-for-sale securities below their cost that are deemed to be other-than-temporary are reflected in earnings as realized losses. In determining whether other-than-temporary impairment (OTTI) exists, management considers many factors, including (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 current liquidity and volatility of the market for each of the individual security categories, (4) the projected cash flows from the specific security type, (5) the financial guarantee and financial rating of the issuer, and (6) the intent and ability of the Credit Union to retain its investment in the issue for a period of time sufficient to allow for any anticipated recovery in fair value. Once a decline in value is determined to be other-than-temporary, and management does not intend to sell the security or it is more likely than not that the Credit Union will not be required to sell the security before recovery, only the portion of the impairment loss representing credit exposure is recognized as a charge to earnings, with the balance recognized as a charge to other comprehensive income. If management intends to sell the security or it is more likely than not that the Credit Union will be required to sell the security before recovering its forecasted cost, the entire impairment loss is recognized as a charge to earnings.

Other investments primarily consist of Federal Home Loan Bank (FHLB) stock and are classified separately and are stated at cost.

FHLB stock: The Credit Union is a member of the FHLB of San Francisco and, as such, is required to maintain a minimum investment in stock of the FHLB that varies with the level of advances outstanding with the FHLB. The stock is bought from and sold to the FHLB based upon its \$100 par value. The stock does not have a readily determinable fair value and, as such, is classified as restricted stock, carried at cost and evaluated for impairment. The stock's value is determined by the ultimate recoverability of the par value rather than by recognizing temporary declines. The determination of whether the par value will ultimately be recovered is influenced by criteria such as the following: (a) the significance of the decline in net assets of the FHLB as compared to the capital stock amount and the length of time this situation has persisted, (b) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance, (c) the impact of legislative and regulatory changes on the customer base of the FHLB, and (d) the liquidity position of the FHLB.

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES AND NATURE OF OPERATIONS (Continued)**

Loans held for sale: Mortgage loans originated and intended for sale in the secondary market are carried at the lower of aggregate cost or fair value, as determined by outstanding commitments from investors. Net unrealized losses, if any, are recorded as a valuation allowance and charged to earnings.

Mortgage loans held for sale are generally sold with servicing rights retained. The carrying value of mortgage loans is reduced by the amount allocated to the servicing right. Gains and losses on sales of mortgage loans are based on the difference between the selling price and the carrying value of the related loan sold.

Mortgage banking derivatives: Commitments to fund mortgage loans (interest rate locks) to be sold into the secondary market and forward commitments for the future delivery of these mortgage loans are accounted for as free standing derivatives. Fair values of these mortgage derivatives are estimated based on changes in mortgage interest rates from the date the interest rate on the loan is locked. As of December 31, 2015 and 2014, management determined these mortgage derivatives were not material.

Loans, net: The Credit Union grants mortgage, commercial and consumer loans to members. In addition, the Credit Union purchases participation loans originated by various other credit unions. Most of these loan participations were purchased without recourse and all are secured by real property. The originating institution performs all servicing functions on these loans.

Loans that the Credit Union has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at their outstanding unpaid principal balances, less an allowance for loan losses and net deferred origination fees and costs. Interest income on loans is recognized over the term of the loan and is calculated using the simple interest method on principal amounts outstanding.

The accrual of interest income on all classes of loans is discontinued at the time the loan is 90 days past due, unless the loan is well-secured and in the process of collection. In addition, interest is not recognized on commercial loans when interest is discontinued and the collection of both principal and interest is considered doubtful. Other personal loans are typically charged off no later than 120 days past-due. Past-due status is based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if the collection of principal and interest is considered doubtful.

All interest accrued, but not collected for loans placed on nonaccrual 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 status. Loans are returned to accrual status when all of 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 cost is recognized as an adjustment to interest income using the interest method over the estimated life of the loans.

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES AND NATURE OF OPERATIONS (Continued)**

Allowance for loan losses: The allowance for loan losses is a valuation allowance for probable incurred credit losses as of the balance sheet date. The allowance is established through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is likely. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review 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 the 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. In addition, regulatory agencies, as an integral part of their examination process, periodically review the Credit Union's allowance for loan losses and may require the Credit Union to make additions to the allowance based on their judgment about information available to them at the time of their examinations.

The Credit Union's allowance for loan losses is the amount considered adequate to absorb probable incurred losses in the portfolio based on management's evaluations of the size and current risk characteristics of the loan portfolio as of the balance sheet date. Such evaluations consider prior and potential loss experience, the risk rating and the levels of impaired and nonperforming 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 original contractual terms of the loan agreement. Specific allowances for loan losses are established for impaired loans on an individual basis as required by the Codification. The specific allowances established for these loans are based on a thorough analysis of the most probable source of repayment, including the present value of the loan's expected future cash flow, the loan's estimated market value or the estimated fair value of the underlying collateral, less costs to sell.

General allowances are established for loans that can be grouped into pools based on similar characteristics as required by the Codification, and accordingly, they are not included in the separately identified impairment disclosures. The general reserve component of the allowance for loan losses also consists of reserve factors that are based on management's assessment of the following for each class: (1) inherent credit risk, (2) historical losses experienced by the Credit Union during the previous twelve months and (3) other qualitative factors. These reserve factors are inherently subjective and are driven by the repayment risk associated with each portfolio segment described below.

*Residential real estate* – The degree of risk in residential real estate lending depends primarily on the loan amount in relation to collateral value, the interest rate and the borrower's ability to repay in an orderly fashion. Economic trends determined by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans. Weak economic trends may indicate that the borrowers' capacity to repay their obligations may be deteriorating.

*Commercial* – Commercial loans generally possess a lower inherent risk of loss than real estate portfolio segments because these loans are generally underwritten to existing cash flows of operating businesses. Debt coverage is provided by operating cash flows. Economic trends influenced by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans. Commercial real estate mortgage loans generally possess a higher inherent risk of loss than other real estate portfolio segments. Adverse economic developments or an overbuilt market impact commercial real estate projects and may result in troubled loans. Trends in vacancy rates of commercial properties impact the credit quality of these loans. High vacancy rates reduce operating revenues and the ability for properties to produce sufficient cash flow to service debt obligations.

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES AND NATURE OF OPERATIONS (Continued)**

*Vehicle* – Vehicle loans are generally underwritten based on the creditworthiness of the borrowers and are secured by vehicles. Economic trends determined by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans. Weak economic trends may indicate that the borrowers' capacity to repay their obligations may be deteriorating.

*Credit card and other consumer loans* – Credit card and other consumer loans are generally unsecured and possess a higher risk of loss than other classes of loans. Economic trends determined by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans. Weak economic trends may indicate that the borrowers' capacity to repay their obligations may be deteriorating.

Troubled debt restructurings: The Credit Union performs a loan-level valuation of those loans identified as troubled debt restructurings. The Credit Union believes that each loan included in the analysis constitutes a troubled debt restructuring when, prior to the restructuring, the borrower experiences financial difficulty and, in response, the Credit Union grants a concession to the borrower, such as a reduction of interest rate, extension of the loan term or other concession that the Credit Union would not otherwise consider. The Credit Union estimates the impairment of the troubled debt restructured loan either by discounting expected future cash flows using the loan's original interest rate or by taking the difference between the loan balance and the collateral value, less selling costs, of the property securing the loan. The amounts are then reserved for as part of the allowance for loan loss account.

Loan servicing: Servicing assets are recognized as separate assets when rights are acquired through the purchase or sale of financial assets. For sales of mortgage loans where servicing is retained, a portion of the cost of originating the loan is allocated to the servicing right based on fair value. Fair value is based on market prices for comparable mortgage servicing contracts, when available, or alternatively on a valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate, ancillary income, prepayment speeds, and default rates and losses. Capitalized servicing rights are reported in other assets and are amortized into noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets.

Servicing assets are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. Impairment is determined by stratifying rights into tranches based on predominant risk characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual tranche, to the extent that fair value is less than the capitalized amount for the tranche. The valuation allowance is reported in other assets. If the Credit Union later determines that all or a portion of the impairment no longer exists for a particular tranche, a reduction of the allowance may be recorded as an increase to income.

Servicing fee income is recorded for fees earned for servicing loans and is included in loan fees. The fees are based on a contractual percentage of the outstanding principal, or a fixed amount per loan and are recorded as income when earned. The amortization of mortgage servicing rights is netted against loan servicing fee income.

Other real estate owned: Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value less cost to sell at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in operating expenses.

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES AND NATURE OF OPERATIONS (Continued)**

Property and equipment: Land is carried at cost. Buildings, leasehold improvements, and furniture and equipment are carried at cost, less accumulated depreciation and amortization. Buildings, furniture and equipment are depreciated using the straight-line method over the estimated useful lives of the assets. The cost of leasehold improvements is amortized using the straight-line method over the lesser of the term of the related lease or the life of the asset.

Transfers of financial assets: Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when the assets have been isolated from the Credit Union, the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and the Credit Union does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity or the ability to unilaterally cause the holder to return specific assets.

Company-owned life insurance: The Credit Union has purchased life insurance policies on certain key executives. Company-owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement.

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 federally insured credit union in an amount equal to 1 percent of its insured members' shares. The deposit would be refunded to the credit union if its insurance coverage is terminated, if it converts its insurance coverage to another source, or if management of the fund is transferred from the NCUA Board.

Goodwill and other intangible assets: Identifiable assets, liabilities and contingent liabilities in entities acquired are measured at fair value at the date of acquisition. Identifiable intangible assets are recognized if they can be separated or arise from a contractual right and the fair value can be reliably measured. Any excess of the cost of business combination over the fair value of the acquired identifiable assets, liabilities and contingent liabilities is recognized as goodwill. Goodwill is assessed for impairment at least annually, and more frequently if events or changes in circumstance indicate that the carrying value may not be recoverable. Goodwill is the only intangible asset with an indefinite life on the statements of financial condition. Other intangible assets consist of the premium recognized on the value of a book of client investment accounts acquired during the year, which is amortized over the estimated life of the asset and is evaluated for impairment on at least an annual basis.

Unfunded commitments and related financial instruments: Financial instruments include off-balance sheet credit instruments, such as commitments to make loans, issued to meet member financing needs. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay. Such financial instruments are recorded on the balance sheet when they are funded.

Members' shares: Members' shares are the savings deposit accounts of the owners of the Credit Union. Share ownership entitles the members to vote in the annual elections of the Board of Directors and on other corporate matters. Irrespective of the amount of shares owned, no member has more than one vote. Members' shares are subordinated to all other liabilities of the Credit Union upon liquidation.

Dividends on members' shares are based on available earnings at the end of a dividend period and are not guaranteed by the Credit Union. Dividend rates are set by the Credit Union's Board of Directors.

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES AND NATURE OF OPERATIONS (Continued)**

Advertising costs: Advertising costs are expensed as incurred.

Income taxes: The Credit Union is exempt, by statute, from federal income taxes. The Credit Union is a state-chartered credit union described in Internal Revenue Code (IRC) Section 501(c)(14). As such, the Credit Union is exempt from federal taxation of income derived from the performance of activities that are in furtherance of its exempt purposes. However, the Credit Union is subject to unrelated business income tax.

FASB Codification Topic 740, *Income Taxes*, provides guidance for how uncertain tax positions should be recognized, measured, disclosed and presented in the financial statements. This requires the evaluation of tax positions taken or expected to be taken in the course of preparing the Credit Union's tax returns to determine whether the tax positions are more likely than not to be sustained "when challenged" or "when examined" by the applicable tax authority. Tax positions not deemed to meet the more-likely-than-not threshold would be recorded as a tax expense and liability in the current year. For the years ended December 31, 2015 and 2014, management has determined that there are no material uncertain tax positions.

Retirement plans: Employee 401(k) and profit sharing plan expense is the amount of matching contributions. Deferred compensation and supplemental retirement plan expense allocates the benefits over years of service.

Comprehensive income: Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the members' equity section of the statements of financial condition.

Fair value of financial instruments: Fair values of financial instruments are estimated using relevant market information and other assumptions as more fully disclosed in a separate note. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect these estimates.

Loss contingencies: Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management was not aware of any loss contingencies that will have a material effect on the financial statements.

Reclassifications: Certain reclassifications have been made to prior years' balances to conform to classifications used in 2015. Reclassifications had no effect on prior years' net income or members' equity.

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES AND NATURE OF OPERATIONS (Continued)**

Recently issued financial accounting pronouncements:

*Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure*

In January 2014, the Financial Accounting Standards Board ("FASB") issued FASB Accounting Standards Update (the "Update") 2014-04, *Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans Upon Foreclosure*. Under this Update, FASB amended existing guidance to clarify when a creditor should be considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan such that the loan should be derecognized and the real estate recognized. These amendments clarify that an in substance repossession or foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either:

- (1) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure, or
- (2) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement.

The amendments in this Update were effective for annual reporting periods beginning after December 15, 2014, including interim periods within that reporting period. The effects of adopting this Update did not have a material effect on the Credit Union's financial position, results of operations or cash flows.

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(Continued)



**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

**NOTE 2 – INVESTMENTS**

Investments classified as available-for-sale consist of the following (in thousands):

<u>December 31, 2015</u>	<u>Amortized Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>
U.S. Government sponsored agency securities	\$ 470,316	\$ 1,655	\$ (1,456)	\$ 470,515
U.S. Government sponsored agency collateralized mortgage obligations, residential	5,987	34	(8)	6,013
U.S. Government sponsored agency mortgage backed securities, residential	<u>16,273</u>	<u>68</u>	<u>(18)</u>	<u>16,323</u>
	<u>\$ 492,576</u>	<u>\$ 1,757</u>	<u>\$ (1,482)</u>	<u>\$ 492,851</u>

<u>December 31, 2014</u>	<u>Amortized Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>
U.S. Government sponsored agency securities	\$ 477,380	\$ 4,002	\$ (2,146)	\$ 479,236
U.S. Government sponsored agency collateralized mortgage obligations, residential	9,676	93	(40)	9,729
U.S. Government sponsored agency mortgage backed securities, residential	<u>23,262</u>	<u>247</u>	<u>(5)</u>	<u>23,504</u>
	<u>\$ 510,318</u>	<u>\$ 4,342</u>	<u>\$ (2,191)</u>	<u>\$ 512,469</u>

Investments by maturity as of December 31, 2015 are summarized as follows (in thousands):

	<u>Available-for-Sale</u>		
	<u>Amortized Cost</u>	<u>Fair Value</u>	<u>Other</u>
No contractual maturity	\$ -	\$ -	\$ 9,740
Less than one year maturity	86,998	87,424	-
One to five years maturity	383,318	383,091	-
Five to ten years maturity	-	-	-
U.S. Government sponsored agency collateralized mortgage obligations, residential	5,987	6,013	-
U.S. Government sponsored agency mortgage-backed securities, residential	<u>16,273</u>	<u>16,323</u>	<u>-</u>
	<u>\$ 492,576</u>	<u>\$ 492,851</u>	<u>\$ 9,740</u>

(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

**NOTE 2 - INVESTMENTS (Continued)**

Expected maturities of U.S. Government sponsored agency collateralized mortgage obligations and U. S. Government sponsored agency mortgage-backed securities may differ from contractual maturities because borrowers may have the right to call or prepay the obligations and are therefore classified separately with no specific maturity date. FHLB stock has been classified with no contractual maturity.

Gross unrealized losses and fair value by length of time that the individual securities have been in a continuous unrealized loss position were as follows (in thousands):

	<u>Fair Value Associated With Unrealized Losses Existing for:</u>		<u>Continuous Unrealized Losses Existing for:</u>		<u>Total Unrealized Losses</u>
	<u>Less Than 12 Months</u>	<u>More Than 12 Months</u>	<u>Less Than 12 Months</u>	<u>More Than 12 Months</u>	
<u>December 31, 2015</u>					
Available-for-sale:					
U.S. Government sponsored agency securities, collateralized mortgage obligations, mortgage-backed securities, residential	\$ 240,899	\$ 30,122	\$ (1,097)	\$ (385)	\$ (1,482)
<u>December 31, 2014</u>					
Available-for-sale:					
U.S. Government sponsored agency securities, collateralized mortgage obligations, mortgage-backed securities, residential	\$ 71,218	\$ 124,950	\$ (304)	\$ (1,887)	\$ (2,191)

At December 31, 2015, the investment portfolio included 89 securities, 50 of which have current unrealized losses that have existed for less than one year and 7 of which have unrealized losses that have existed for more than one year. All of these securities were considered to be acceptable credit risks. Based upon an evaluation of the available evidence, including recent changes in market interest rates, credit rating information and information obtained from regulatory filings, management believes the decline in fair value for these securities is temporary. In addition, the Credit Union has the intent and ability to hold these investment securities for a period of time sufficient to allow for an anticipated recovery.

The Credit Union did not have any other-than-temporary impairment in 2015 in available-for-sale securities.

(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 2 - INVESTMENTS** (Continued)

Other investments consist of the following at December 31 (in thousands):

	<u>2015</u>	<u>2014</u>
FHLB stock	\$ 9,683	\$ 9,683
Other investments	<u>57</u>	<u>57</u>
	<u>\$ 9,740</u>	<u>\$ 9,740</u>

The fair value of other investments and FHLB stock is not practical to determine due to restrictions placed on its transferability.

The Credit Union views its investment in the FHLB stock as a long-term investment. The FHLB of San Francisco released annual financial statements as of December 31, 2015 and 2014, disclosing that the FHLB of San Francisco was in compliance with all its regulatory capital requirements and has paid quarterly dividends during 2015 and 2014. With consideration given to these factors, management concluded that the stock was not impaired at December 31, 2015 or 2014.

Securities totaling \$30,782,000 have been pledged as collateral to secure State of California Treasury Deposits as disclosed in Note 7. Securities totaling \$51,249,000 have been pledged as collateral to secure FHLB advances as more fully disclosed in Note 8.

**NOTE 3 - LOANS, NET**

Loans consist of the following at December 31 (in thousands):

	<u>2015</u>	<u>2014</u>
Residential real estate	\$ 612,946	\$ 506,532
Commercial	128,242	111,933
Vehicle	608,274	547,042
Credit card and other consumer	<u>93,269</u>	<u>91,344</u>
Loans receivable, gross	1,442,731	1,256,851
Deferred net loan origination costs	5,625	3,470
Allowance for loan losses	<u>(16,162)</u>	<u>(16,820)</u>
	<u>\$ 1,432,194</u>	<u>\$ 1,243,501</u>

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 3 - LOANS, NET (Continued)**

The following presents, by portfolio segment, the changes in the allowance for loan losses and the recorded investment in loans for the years ended December 31, 2015 and 2014 (in thousands):

<u>December 31, 2015</u>	<u>Residential Real Estate</u>	<u>Commercial</u>	<u>Vehicle</u>	<u>Credit Card and Other Consumer</u>	<u>Total</u>
Allowance for loan losses:					
Beginning balance	\$ 7,931	\$ 3,720	\$ 3,150	\$ 2,019	\$ 16,820
Provision for loan losses	(1,251)	1,055	1,869	2,624	4,297
Charge-offs	(559)	(966)	(2,334)	(2,348)	(6,207)
Recoveries	<u>415</u>	<u>21</u>	<u>651</u>	<u>165</u>	<u>1,252</u>
Ending Balance	<u>\$ 6,536</u>	<u>\$ 3,830</u>	<u>\$ 3,336</u>	<u>\$ 2,460</u>	<u>\$ 16,162</u>
<u>December 31, 2014</u>	<u>Residential Real Estate</u>	<u>Commercial</u>	<u>Vehicle</u>	<u>Credit Card and Other Consumer</u>	<u>Total</u>
Allowance for loan losses:					
Beginning balance	\$ 9,648	\$ 5,144	\$ 2,963	\$ 2,326	\$ 20,081
Provision for loan losses	(1,103)	2,369	2,045	1,814	5,125
Charge-offs	(845)	(3,801)	(2,117)	(2,552)	(9,315)
Recoveries	<u>231</u>	<u>8</u>	<u>259</u>	<u>431</u>	<u>929</u>
Ending Balance	<u>\$ 7,931</u>	<u>\$ 3,720</u>	<u>\$ 3,150</u>	<u>\$ 2,019</u>	<u>\$ 16,820</u>

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

**NOTE 3 - LOANS, NET (Continued)**

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment based on impairment method as of December 31, 2015 and 2014:

<u>December 31, 2015</u>	<u>Residential Real Estate</u>	<u>Commercial</u>	<u>Vehicle</u>	<u>Credit Card and Other Consumer</u>	<u>Total</u>
Allowance for loan losses:					
Ending balance attributable to loans:					
Individually evaluated for impairment	\$ 5,988	\$ 3,830	\$ 35	\$ 43	\$ 9,896
Collectively evaluated for impairment	<u>548</u>	<u>-</u>	<u>3,301</u>	<u>2,417</u>	<u>6,266</u>
Total ending allowance balance	<u>\$ 6,536</u>	<u>\$ 3,830</u>	<u>\$ 3,336</u>	<u>\$ 2,460</u>	<u>\$ 16,162</u>
Loans:					
Loans individually evaluated for impairment	\$ 47,959	\$ 14,402	\$ 1,271	\$ 224	\$ 63,856
Loans collectively evaluated for impairment	<u>564,987</u>	<u>113,840</u>	<u>607,003</u>	<u>93,045</u>	<u>1,378,875</u>
Total ending gross loans balance	<u>\$ 612,946</u>	<u>\$ 128,242</u>	<u>\$ 608,274</u>	<u>\$ 93,269</u>	<u>\$ 1,442,731</u>
<u>December 31, 2014</u>	<u>Residential Real Estate</u>	<u>Commercial</u>	<u>Vehicle</u>	<u>Credit Card and Other Consumer</u>	<u>Total</u>
Allowance for loan losses:					
Ending balance attributable to loans:					
Individually evaluated for impairment	\$ 7,258	\$ 3,276	\$ 103	\$ 55	\$ 10,692
Collectively evaluated for impairment	<u>673</u>	<u>444</u>	<u>3,047</u>	<u>1,964</u>	<u>6,128</u>
Total ending allowance balance	<u>\$ 7,931</u>	<u>\$ 3,720</u>	<u>\$ 3,150</u>	<u>\$ 2,019</u>	<u>\$ 16,820</u>
Loans:					
Loans individually evaluated for impairment	\$ 51,553	\$ 13,355	\$ 1,796	\$ 195	\$ 66,899
Loans collectively evaluated for impairment	<u>454,979</u>	<u>98,578</u>	<u>545,246</u>	<u>91,149</u>	<u>1,189,952</u>
Total ending gross loans balance	<u>\$ 506,532</u>	<u>\$ 111,933</u>	<u>\$ 547,042</u>	<u>\$ 91,344</u>	<u>\$ 1,256,851</u>

The allowance for loan losses was considered by the Credit Union as adequate to cover probable incurred losses in the loan portfolio as of the balance sheet date. However, no assurance can be given that the Credit Union, in any particular period, will not sustain loan losses that exceed the allowance, or that subsequent evaluation of the loan portfolio, in light of then-prevailing factors, including economic conditions, credit quality of the assets comprising the portfolio, and the ongoing evaluation process, will not require significant changes in the allowance for loan losses.

(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

**NOTE 3 - LOANS, NET (Continued)**

The following presents the recorded investment and unpaid principal balance for impaired loans with associated allowance amount, if applicable, as of December 31, 2015 and 2014 (in thousands). The recorded investment in loans includes accrued interest receivable and loan origination fees, net.

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
<b>December 31, 2015</b>					
Impaired loans with an allowance:					
Residential real estate	\$ 32,691	\$ 32,332	\$ 5,988	\$ 38,646	\$ 1,670
Commercial	9,196	9,107	3,830	11,276	299
Vehicle	527	522	35	992	58
Credit card and other consumer	200	198	43	195	10
	<u>\$ 42,614</u>	<u>\$ 42,159</u>	<u>\$ 9,896</u>	<u>\$ 51,109</u>	<u>\$ 2,037</u>
Impaired loans without an allowance:					
Residential real estate	\$ 15,268	\$ 15,147	-	\$ 11,111	\$ 254
Commercial	5,206	5,187	-	2,603	-
Vehicle	744	741	-	541	12
Credit card and other consumer	24	24	-	14	-
	<u>\$ 21,242</u>	<u>\$ 21,099</u>	<u>\$ -</u>	<u>\$ 14,269</u>	<u>\$ 266</u>
Totals:					
Residential real estate	\$ 47,959	\$ 47,479	\$ 5,988	\$ 49,757	\$ 1,924
Commercial	14,402	14,294	3,830	13,879	299
Vehicle	1,271	1,263	35	1,533	70
Credit card and other consumer	224	222	43	209	10
	<u>\$ 63,856</u>	<u>\$ 63,258</u>	<u>\$ 9,896</u>	<u>\$ 65,378</u>	<u>\$ 2,303</u>
<b>December 31, 2014</b>					
Impaired loans with an allowance:					
Residential real estate	\$ 44,600	\$ 44,232	\$ 7,258	\$ 43,012	\$ 1,806
Commercial	13,355	13,236	3,276	16,084	250
Vehicle	1,456	1,446	103	1,851	84
Credit card and other consumer	192	190	55	616	8
	<u>\$ 59,603</u>	<u>\$ 59,104</u>	<u>\$ 10,692</u>	<u>\$ 61,563</u>	<u>\$ 2,148</u>
Impaired loans without an allowance:					
Residential real estate	\$ 6,953	\$ 6,892	-	\$ 10,089	\$ 261
Commercial	-	-	-	-	-
Vehicle	340	337	-	712	26
Credit card and other consumer	3	4	-	114	-
	<u>\$ 7,296</u>	<u>\$ 7,233</u>	<u>\$ -</u>	<u>\$ 10,915</u>	<u>\$ 287</u>
Totals:					
Residential real estate	\$ 51,553	\$ 51,124	\$ 7,258	\$ 53,101	\$ 2,067
Commercial	13,355	13,236	3,276	16,084	250
Vehicle	1,796	1,783	103	2,563	110
Credit card and other consumer	195	194	55	730	8
	<u>\$ 66,899</u>	<u>\$ 66,337</u>	<u>\$ 10,692</u>	<u>\$ 72,478</u>	<u>\$ 2,435</u>

(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 3 - LOANS, NET (Continued)**

Interest income recorded on a cash basis was not material during the years ended December 31, 2015 and 2014.

**Troubled Debt Restructurings:**

During the periods ending December 31, 2015 and 2014, the terms of certain loans were modified as troubled debt restructurings. The modifications of the terms of such loans included one or a combination of the following: a reduction of the stated interest rate or an extension of the maturity date.

During the twelve month periods ending December 31, 2015 and 2014, modifications involving an extension of the maturity date were for periods ranging from three months up to 12 years. Modifications involving a reduction of the stated interest rate of the loan included reductions in rate of between 0% and 3%.

The following tables show additional information on new troubled debt restructures including those that subsequently defaulted within twelve months following modification during the years ended December 31, 2015 and 2014 (in thousands):

<u>December 31, 2015</u>	<u>Number of Contracts</u>	<u>Pre-Modification Outstanding Recorded Investments</u>	<u>Post-Modification Outstanding Recorded Investments</u>
TDRs occurring during the year:			
Residential real estate	18	\$ 2,973	\$ 2,901
Commercial	7	11,623	10,798
Vehicle	22	400	397
Credit card and other consumer	15	404	393
	<u>62</u>	<u>\$ 15,400</u>	<u>\$ 14,489</u>
	<u>Number of Contracts</u>	<u>Recorded Investments</u>	
TDRs that subsequently defaulted:			
Residential real estate	1	\$ 234	
Commercial	-	-	
Vehicle	1	24	
Credit card and other consumer	1	15	
	<u>3</u>	<u>\$ 273</u>	

The troubled debt restructurings occurring during the year increased the allowance for loan losses by \$1,089,000 and resulted in no charge offs during the year ending December 31, 2015. Of the troubled debt restructurings occurring during the year, those that subsequently defaulted accounted for \$6,000 of the increase in the allowance for loan losses and resulted in no charge offs during the year ending December 31, 2015. The Credit Union has not committed to lend additional amounts as of December 31, 2015 to borrowers with outstanding loans that are classified as troubled debt restructurings.

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

**NOTE 3 - LOANS, NET (Continued)**

<u>December 31, 2014</u>	<u>Number of Contracts</u>	<u>Pre-Modification Outstanding Recorded Investments</u>	<u>Post-Modification Outstanding Recorded Investments</u>
TDRs occurring during the year:			
Residential real estate	10	\$ 1,391	\$ 1,876
Commercial	1	3,901	3,901
Vehicle	12	224	224
Credit card and other consumer	<u>19</u>	<u>444</u>	<u>444</u>
	<u>42</u>	<u>\$ 5,960</u>	<u>\$ 6,445</u>
TDRs that subsequently defaulted:			
Residential real estate	1	\$ 68	
Commercial	1	28	
Vehicle	3	60	
Credit card and other consumer	<u>1</u>	<u>10</u>	
	<u>6</u>	<u>\$ 166</u>	

The troubled debt restructurings occurring during the year increased the allowance for loan losses by \$1,136,000 and resulted in no charge offs during the year ending December 31, 2014. Of the troubled debt restructurings occurring during the year, those that subsequently defaulted accounted for \$44,000 of the increase in the allowance for loan losses and resulted in charge offs of \$18,000 during the year ending December 31, 2014.

A loan is considered to be in payment default once it is 30 days contractually past due under the modified terms or charged off.

In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the Credit Union's internal underwriting policy.

**Credit Quality Indicators:**

Management regularly reviews and risk grades commercial loans in the Credit Union's portfolio. The risk grading system allows management to classify assets by credit quality in accordance with the Credit Union policy. The Credit Union's internal risk grading system definitions are as follows:

- Satisfactory—loans which are protected by the current net worth and paying capacity of the obligor(s) or by the value of the underlying collateral.
- Special Mention—loans with potential weaknesses that require close attention. If left uncorrected, the weaknesses may result in deterioration of the repayment prospects for the asset, or in the future loan credit position.

(Continued)



**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 3 - LOANS, NET** (Continued)

- **Substandard**— Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Credit Union will sustain some loss if the deficiencies are not corrected.
- **Doubtful**—A loan classified doubtful has all the weaknesses inherent in one classified substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors that may work to the advantage and strengthening of the loan, its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors include: sale or liquidation actions; other forms of income or assistance; perfecting liens on collateral; and refinancing plans.
- **Loss**—A loan classified as a loss is considered uncollectible and of such little value that its continuance as a loan is not warranted. This classification does not necessarily mean that the loan has absolutely no recovery or salvage value, but rather, it is not practical or desirable to defer writing off this asset even though partial recovery may occur in the future.

The following presents, by credit quality indicator, the commercial portfolio as of December 31, 2015 and 2014 (in thousands):

	2015	2014
Satisfactory	\$ 110,198	\$ 94,486
Special mention	3,785	3,602
Substandard	10,276	9,583
Doubtful	3,983	4,262
Loss	-	-
	\$ 128,242	\$ 111,933

Management reviews the performance of the loan portfolio on a regular basis. Non-commercial loans are evaluated on the basis of performing and nonperforming status. Nonperforming loans are defined as being greater than two months past due.

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

**NOTE 3 - LOANS, NET (Continued)**

The following presents, by credit quality indicator, the residential real estate, vehicle, and consumer loan portfolio as of December 31, 2015 and 2014 (in thousands):

	<u>Performing</u>	<u>Nonperforming</u>	<u>Total</u>
<u>December 31, 2015</u>			
Residential real estate	\$ 608,082	\$ 4,864	\$ 612,946
Vehicle	607,549	725	608,274
Credit card and other consumer	<u>92,504</u>	<u>765</u>	<u>93,269</u>
	<u>\$ 1,308,135</u>	<u>\$ 6,354</u>	<u>\$ 1,314,489</u>
 <u>December 31, 2014</u>			
Residential real estate	\$ 500,730	\$ 5,802	\$ 506,532
Vehicle	546,189	853	547,042
Credit card and other consumer	<u>90,523</u>	<u>821</u>	<u>91,344</u>
	<u>\$ 1,137,442</u>	<u>\$ 7,476</u>	<u>\$ 1,144,918</u>

The following represents an aging analysis of the recorded investment of past due loans as of December 31, 2015 and 2014 (in thousands):

	1 to less Than 2 Months	2 to Less Than 3 Months	3 Months and Greater	Total Past Due	Current	Total Loan Receivable, Gross	Loans on Which Interest Has Been Discontinued
<u>December 31, 2015</u>							
Residential real estate	\$ 2,478	\$ 822	\$ 4,042	\$ 7,342	\$ 605,604	\$ 612,946	\$ 4,042
Commercial	-	16	294	310	127,932	128,242	10,011
Vehicle	5,845	334	391	6,570	601,704	608,274	391
Credit card and other consumer	<u>597</u>	<u>259</u>	<u>506</u>	<u>1,362</u>	<u>91,907</u>	<u>93,269</u>	<u>507</u>
	<u>\$ 8,920</u>	<u>\$ 1,431</u>	<u>\$ 5,233</u>	<u>\$ 15,584</u>	<u>\$ 1,427,147</u>	<u>\$ 1,442,731</u>	<u>\$ 14,951</u>
 <u>December 31, 2014</u>							
Residential real estate	\$ 1,763	\$ 627	\$ 5,175	\$ 7,565	\$ 498,967	\$ 506,532	\$ 5,175
Commercial	167	20	3,911	4,098	107,835	111,933	7,970
Vehicle	4,190	458	395	5,043	541,999	547,042	395
Credit card and other consumer	<u>755</u>	<u>332</u>	<u>489</u>	<u>1,576</u>	<u>89,768</u>	<u>91,344</u>	<u>489</u>
	<u>\$ 6,875</u>	<u>\$ 1,437</u>	<u>\$ 9,970</u>	<u>\$ 18,282</u>	<u>\$ 1,238,569</u>	<u>\$ 1,256,851</u>	<u>\$ 14,029</u>

There were no loans at December 31, 2015 or 2014 that were on accrual status and 90 days or more past due.

(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 4 - LOAN SERVICING**

Mortgage loans serviced for others are not included in the accompanying statements of financial condition. The unpaid principal balances of these loans at December 31 are summarized as follows (in thousands):

	<u>2015</u>	<u>2014</u>
Mortgage loan portfolios serviced for others	\$ 635,755	\$ 603,294

Custodial escrow balances maintained in connection with the foregoing loan servicing, and included in member shares, were \$2,752,000 and \$2,291,000 at December 31, 2015 and 2014, respectively.

Mortgage servicing rights are recorded within other assets on the statements of financial condition. A summary of the changes in the balance of mortgage servicing rights for the years ended December 31 was as follows (in thousands):

	<u>2015</u>	<u>2014</u>
Balance, beginning of the year	\$ 4,114	\$ 3,866
Servicing assets recognized during the year	1,120	835
Amortization of servicing assets	(672)	(575)
Change in valuation allowance	<u>2</u>	<u>(12)</u>
Balance, end of year	<u>\$ 4,564</u>	<u>\$ 4,114</u>
Fair value of mortgage servicing rights	<u>\$ 6,556</u>	<u>\$ 6,156</u>

The aggregate changes in the valuation allowances for mortgage servicing rights for the years ended December 31 were as follows (in thousands):

	<u>2015</u>	<u>2014</u>
Balance, beginning of the year	\$ 12	\$ -
Additions	10	17
Reductions	<u>(12)</u>	<u>(5)</u>
Balance, end of year	<u>\$ 10</u>	<u>\$ 12</u>

The key economic assumptions used in determining the fair value of mortgage servicing rights at December 31 were as follows:

	<u>2015</u>	<u>2014</u>
Prepayment speed	16.38%	15.30%
Weighted-average life (years)	6.59	7.29
Yield to maturity discount rate	9.80%	9.80%

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 5 - PROPERTY AND EQUIPMENT, NET**

Property and equipment at December 31 are summarized as follows (in thousands):

	2015	2014
Land	\$ 8,651	\$ 8,651
Building	43,835	41,902
Leasehold improvements	3,270	3,226
Furniture and equipment	32,662	34,379
	88,418	88,158
Accumulated depreciation and amortization	(33,800)	(34,107)
	\$ 54,618	\$ 54,051

Depreciation expense was \$1,238,000 and \$906,000 for 2015 and 2014.

The Credit Union leases 22 branch offices and automated teller machine locations. The operating leases contain renewal options and provisions requiring the Credit Union to pay property taxes and operating expenses over base time periods. All rental payments are dependent only upon the lapse of time. Minimum rental payments under operating leases with initial or remaining terms of one year or more at December 31, 2015 were as follows (in thousands):

Years Ending December 31,	
2016	\$ 1,153
2017	1,005
2018	761
2019	652
Subsequent Years	369
	\$ 3,940

Rental expense for the years ended December 31, 2015 and 2014, for all facilities leased under operating leases, totaled \$1,510,000 and \$1,485,000 respectively.

**NOTE 6 – GOODWILL AND OTHER INTANGIBLE ASSETS**

The Credit Union completed a merger transaction with American River HealthPro Credit Union that became effective on July 1, 2009. This merger was accounted for as a purchase business combination. As the purpose of this merger was to achieve growth and economies of scale among these mutual enterprises, no payment considerations were involved, contingent or otherwise. The goodwill of \$13,282,000 associated with this merger, arising from expected synergies from the combined operations, for the years ended December 31, 2015 and 2014, is subject to an annual impairment test. Management assesses goodwill for impairment at least annually, and has determined that there was no goodwill impairment for 2015 or 2014.

In 2015, the Credit Union purchased a book of client investment accounts which resulted in an intangible asset of \$196,000 as of December 31, 2015. This intangible will be amortized over a period of 10 years beginning January 2016.

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 7 - MEMBERS' SHARES**

Members' shares at December 31 are summarized as follows (in thousands):

	2015	2014
Regular share accounts	\$ 367,467	\$ 310,216
Share draft accounts	502,009	460,708
Money market accounts	783,184	755,463
Certificate accounts	275,908	285,062
Individual retirement accounts	36,447	35,022
Individual retirement certificate accounts	59,057	61,863
	\$ 2,024,072	\$ 1,908,334

Shares by maturity as of December 31, 2015 are summarized as follows (in thousands):

No contractual maturity	\$ 1,689,107
Zero to one year maturity	177,603
One to two years maturity	64,873
Two to three years maturity	47,895
Three to four years maturity	19,194
Four to five years maturity	25,222
Over five years maturity	178
	\$ 2,024,072

Regular share accounts, share draft accounts, money market accounts and individual retirement accounts have no contractual maturity. Certificate accounts have maturities of six years or less.

The NCUSIF insures members' shares, including individual retirement and Keogh accounts up to \$250,000.

The aggregate amount of members' shares in accounts exceeding \$250,000 as of December 31, 2015 and 2014 were \$3,341,000 and \$2,972,000, respectively.

The aggregate amount of certificates in denominations of \$100,000 or more at December 31, 2015 and 2014 was \$85,330,000 and \$82,558,000, respectively.

The Credit Union maintains public unit share accounts, which consist of State of California, Office of the State Treasurer funds invested in the Credit Union through the Treasurer's Time Deposit program. These funds are subject to immediate withdrawal at maturity and bear interest rate specified by the Office of the State Treasurer. The balance in public unit share accounts was \$25,004,000 and \$5,001,000 at December 31, 2015 and 2014, respectively.

At December 31, 2015 and 2014, overdraft demand shares reclassified to loans totaled \$561,000 and \$495,000, respectively.

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 8 - BORROWINGS**

The Credit Union utilizes a demand loan agreement with the FHLB. The terms of the agreement call for pledging certain investments held in safekeeping by the FHLB and/or a portion of the Credit Union's real estate loan portfolio. As of December 31, 2015 the pledged assets included securities totaling \$51,249,000 and no real estate loans. The agreement provides for a maximum available borrowing amount of 25% of assets or \$574,000,000. At December 31, 2015 and 2014, there were no borrowings under this agreement. The agreement is reviewed for continuation by the FHLB and the Credit Union annually.

The Credit Union is authorized to use the Discount Window with the Federal Reserve Bank of San Francisco (FRBSF) to borrow money on the terms and security required per the FRBSF's Operating Circular No 10, effective October 15, 2006, as amended and supplemented from time to time thereafter ("OC-10"). The agreement is reviewed for continuation by the FRBSF and the Credit Union annually.

**NOTE 9 - OFF-BALANCE-SHEET ACTIVITIES**

The Credit Union is party to conditional commitments to lend funds in the normal course of business to meet the financing needs of its members. These commitments represent financial instruments to extend credit, which include lines of credit, credit cards and home equity lines that involve, to varying degrees, elements of credit and interest rate risk in excess of amounts recognized in the financial statements.

The Credit Union's exposure to credit loss is represented by the contractual amount of these commitments. The Credit Union follows the same credit policies in making commitments as it does for those loans recorded in the financial statements.

The credit union has approved residential real estate loans in processing that were not yet funded at December 31, 2015 and 2014 of \$7,414,000 and \$1,530,000, respectively.

Unfunded loan commitments under lines of credit are summarized as follows (in thousands):

	<u>2015</u>	<u>2014</u>
Residential real estate	\$ 34,902	\$ 40,967
Commercial	4,476	4,629
Credit card and other consumer	<u>194,015</u>	<u>173,688</u>
	<u>\$ 233,393</u>	<u>\$ 219,284</u>

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 9 - OFF-BALANCE-SHEET ACTIVITIES (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 and may require payment of a fee. Because many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Credit Union evaluates each member's creditworthiness on a case-by-case basis. The amount of collateral obtained to secure borrowing on the lines of credit is based on management's credit evaluation of the member.

Unfunded commitments under revolving credit lines and overdraft protection agreements are commitments for possible future extensions of credit to existing customers. These lines of credit are uncollateralized, usually do not contain a specified maturity date and ultimately may not be drawn upon to the total extent to which the Credit Union is committed.

**NOTE 10 - COMMITMENTS AND CONTINGENT LIABILITIES**

The Credit Union is party to various legal actions normally associated with collections of loans and other business activities of financial institutions, the aggregate effect of which, in management's opinion, would not have a material adverse effect on the financial condition or results of operations of the Credit Union.

**NOTE 11 - EMPLOYEE BENEFITS**

The Credit Union has a defined-contribution 401(k) benefit and profit sharing plan and 457(b) plan that allow substantially all employees to defer a portion of their salary into the plans. The Credit Union is not required to make matching and profit sharing contributions to the plan. Benefit plan and profit sharing plan costs are accrued and funded on a current basis. The Credit Union voluntarily contributed \$2,331,000 and \$2,099,000 to the benefit plans for the years ended December 31, 2015 and 2014, respectively.

The Credit Union maintains supplemental executive retirement plans to provide certain retirement benefits for key executives. The contributions into the plans are accrued as compensation expense and funded on a current basis. The expense recognized under these plans was \$712,000 for each of the years ended December 31, 2015 and 2014. The Credit Union has \$74,000 accrued under these plans at December 31, 2015.

The Credit Union recognized \$3,043,000 and \$2,811,000 in compensation and benefit expense for all plans for the years ended December 31, 2015 and 2014, respectively.

**NOTE 12 - MEMBERS' EQUITY**

The Credit Union is subject to various regulatory capital requirements administered by the NCUA and the California Department of Business Oversight. 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 guidelines and the regulatory framework for prompt corrective action, the Credit Union must meet specific capital guidelines that involve quantitative measures of the Credit Union's assets, liabilities and certain off-balance-sheet items as calculated under GAAP. The Credit Union's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 12 - MEMBERS' EQUITY (Continued)**

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 to total assets. Further, credit unions over \$10,000,000 in assets are also required to calculate a Risk-Based Net Worth (RBNW) requirement, which establishes whether or not the Credit Union will be considered "complex" under the regulatory framework. The Credit Union's RBNW requirements as of December 31, 2015 and 2014 were 5.24 percent and 5.37 percent, respectively. The minimum requirement to be considered "complex" under the regulatory framework is 6 percent. Management believes, as of December 31, 2015 and 2014, that the Credit Union met all regulatory capital adequacy requirements to which it is subject.

Other appropriated retained earnings represent a restriction of retained earnings as established by the Board of Directors.

As of December 31, 2015 and 2014, 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 percent of assets. There were no conditions or events since that notification that management believes have changed the Credit Union's category.

The Credit Union's actual capital amounts and ratios at December 31 were as follows (in thousands):

	2015		2014	
	Amount	Ratio/ Requirement	Amount	Ratio/ Requirement
Amount needed to be classified as adequately capitalized	\$ 136,926	6.00%	\$ 128,258	6.00%
Amount needed to be classified as well-capitalized	159,746	7.00%	149,634	7.00%
Actual net worth	216,986	9.51%	207,581	9.71%

Because the RBNW requirement was less than the net worth ratio, the Credit Union retained its original category. Further, in performing its calculation of total assets, the Credit Union used the quarter-end balance option, as permitted by regulation.

**NOTE 13 - RELATED-PARTY TRANSACTIONS**

In the normal course of business, the Credit Union extends credit to directors, Supervisory Committee members and executive officers. The aggregate loans to related parties at December 31, 2015 and 2014 were \$4,031,000 and \$5,408,000, respectively. Member shares from related parties at December 31, 2015 and 2014 amounted to \$7,148,000 and \$7,822,000, respectively.

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(Continued)



**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 14 - FAIR VALUE**

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices such as 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.

Level 3: Significant unobservable inputs that reflect a company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The following methods and assumptions were used by the Credit Union in estimating fair values as disclosed herein:

Cash and cash equivalents: The carrying amounts of cash and cash equivalents approximate their fair value.

Investments available-for-sale: The fair value of investment securities is the market value based on quoted market prices, when available, or market prices provided by recognized broker-dealers. If listed prices or quotes are not available, fair value is based upon externally developed models that use unobservable inputs due to the limited market activity of the instrument.

Other investments, including FHLB stock: It is not practical to determine the fair value of FHLB stock and other investments due to restrictions placed on its transferability.

Loans held for sale: The carrying amount of loans held for sale approximates fair value, which is estimated based upon binding contracts and quotes from investors.

Loans, net: Fair values of loans, excluding loans held for sale, are estimated as follows: For variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Impaired loans are valued at the lower of cost or fair value as described later in this footnote. The methods utilized to estimate the fair value of loans do not necessarily represent an exit price.

Accrued interest receivable and payable: Accrued interest represents interest on loans, investments and share accounts. The carrying amount of accrued interest receivable and payable approximates fair value.

Members' shares and public unit shares: The fair value of shares payable upon demand (regular shares, share draft and money market accounts) is the amount payable at the date of the statement of financial condition. The fair value of fixed maturity accounts (share certificates, IRA share accounts and public unit shares) is estimated by discounting the estimated cash flows using interest rates for comparable instruments.

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 14 - FAIR VALUE** (Continued)

Off-balance-sheet, credit-related instruments: Fair values for off-balance-sheet, credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. The fair value for such financial instruments is not material.

Fair value of financial instruments: The table below presents the carrying value and fair value of the Credit Union's financial instruments at December 31 (in thousands):

	2015		2014	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash and cash equivalents	\$ 149,831	\$ 149,831	\$ 180,266	\$ 180,266
Investments available-for-sale	492,851	492,851	512,469	512,469
Other investments	9,740	N/A	9,740	N/A
Loans held for sale	5,559	5,559	1,618	1,618
Loans, net	1,432,194	1,439,278	1,243,501	1,256,408
Accrued interest receivable	5,577	5,577	5,874	5,874
Financial liabilities:				
Members' shares	\$ 2,024,072	\$ 2,009,959	\$ 1,908,334	\$ 1,910,676
Public unit shares	25,004	25,001	5,001	5,000

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 14 - FAIR VALUE** (Continued)

Fair value on a recurring basis: The following table summarizes assets and liabilities measured at fair value on a recurring basis as of December 31, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value (in thousands):

<u>Assets</u>	2015			
	<u>Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
U.S. Government sponsored agency securities	\$ 470,515	\$ -	\$ 470,515	\$ -
U.S. Government sponsored agency collateralized mortgage obligations, residential	6,013	-	6,013	-
U.S. Government sponsored agency mortgage-backed securities, residential	<u>16,323</u>	<u>-</u>	<u>16,323</u>	<u>-</u>
	<u>\$ 492,851</u>	<u>\$ -</u>	<u>\$ 492,851</u>	<u>\$ -</u>

<u>Assets</u>	2014			
	<u>Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
U.S. Government sponsored agency securities	\$ 479,236	\$ -	\$ 479,236	\$ -
U.S. Government sponsored agency collateralized mortgage obligations, residential	9,729	-	9,729	-
U.S. Government sponsored agency mortgage-backed securities, residential	<u>23,504</u>	<u>-</u>	<u>23,504</u>	<u>-</u>
	<u>\$ 512,469</u>	<u>\$ -</u>	<u>\$ 512,469</u>	<u>\$ -</u>

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
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**NOTE 14 - FAIR VALUE (Continued)**

Fair value on a nonrecurring basis: Certain assets and liabilities are measured at fair value on a nonrecurring basis. The instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). The following table presents the assets and liabilities carried on the statement of financial condition, by class and by level within the valuation hierarchy (as described above), for which a nonrecurring change in fair value has been recorded (in thousands):

	2015				Total Losses
	Fair Value	Level 1	Level 2	Level 3	
Impaired loans:					
Commercial	\$ 4,309	\$ -	\$ -	\$ 4,309	\$ 1,510
Residential real estate	<u>1,648</u>	<u>-</u>	<u>1,648</u>	<u>-</u>	<u>156</u>
Total impaired loans	<u>5,957</u>	<u>-</u>	<u>1,648</u>	<u>4,309</u>	<u>1,666</u>
Other real estate owned:					
Commercial	2,361	-	-	2,361	356
Residential real estate	<u>524</u>	<u>-</u>	<u>-</u>	<u>524</u>	<u>-</u>
Total other real estate owned	<u>2,885</u>	<u>-</u>	<u>-</u>	<u>2,885</u>	<u>356</u>
	<u>\$ 8,842</u>	<u>\$ -</u>	<u>\$ 1,648</u>	<u>\$ 7,194</u>	<u>\$ 2,022</u>
	2014				
	Fair Value	Level 1	Level 2	Level 3	Total Losses
Impaired loans:					
Commercial	\$ 8,686	\$ -	\$ -	\$ 8,686	\$ 207
Residential real estate	<u>2,953</u>	<u>-</u>	<u>2,953</u>	<u>-</u>	<u>318</u>
Total impaired loans	<u>11,639</u>	<u>-</u>	<u>2,953</u>	<u>8,686</u>	<u>525</u>
Other real estate owned:					
Commercial	3,446	-	-	3,446	3,710
Residential real estate	<u>206</u>	<u>-</u>	<u>-</u>	<u>206</u>	<u>154</u>
Total other real estate owned	<u>3,652</u>	<u>-</u>	<u>-</u>	<u>3,652</u>	<u>3,864</u>
	<u>\$ 15,291</u>	<u>\$ -</u>	<u>\$ 2,953</u>	<u>\$ 12,338</u>	<u>\$ 4,389</u>

(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

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**NOTE 14 - FAIR VALUE (Continued)**

Impaired Loans: The Credit Union records loans at fair value on a non-recurring basis. The fair value of impaired loans is estimated by either an observable market price (if available) or the fair value of the underlying collateral, if collateral dependent. The fair value of collateral is determined periodically by third party asset valuation models for residential loans and appraisals (by licensed appraisers) for commercial loans. Impaired loans where an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. Asset valuation models conducted on collateral securing residential loans utilize a market approach and contain no unobservable market data. Therefore, such asset valuation models are classified as Level 2 in the fair value hierarchy. Appraisals conducted on collateral securing commercial loans utilize a market, income, or cost approach or some combination of the three and typically contain unobservable market data. Therefore, such appraisals are classified as Level 3 in the fair value hierarchy. Unobservable market data contained in appraisals often includes adjustments to comparable property sales for such items as location, size and quality. Unobservable market data also includes liquidation discounts estimated by appraisers or management. Impaired loans evaluated under the discounted cash flow method are excluded from the fair value table for non-recurring assets. The discounted cash flow method is not a fair value measurement since the discount rate utilized is the loan's effective interest rate which is not a market rate.

Other Real Estate Owned: The Credit Union records other real estate owned at fair value on a non-recurring basis using third party appraisals. Appraisals conducted on other real estate owned utilize a market, income, or cost approach or some combination of the three and typically contain unobservable market data. Therefore, such appraisals are classified as Level 3 in the fair value hierarchy. Unobservable market data contained in appraisals often includes adjustments to comparable property sales for such items as location, size and quality. Unobservable market data also includes liquidation discounts estimated by appraisers or management.

Appraisals for both collateral-dependent impaired loans and real estate owned are performed by certified general appraisers (for commercial properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by the Credit Union. For commercial properties, the Credit Union reviews the assumptions and approaches utilized in the appraisal to determine the reasonableness of the overall resulting fair value. For residential properties, the appraised value is compared to other sources including Broker Price Opinions and Automated Valuation Models to validate the reasonableness of the appraised amount. On an annual basis, the Credit Union obtains an updated appraisal for collateral-dependent impaired loans and real estate owned properties and compares the actual selling price of collateral that has been sold to the most recent appraised value to determine what additional adjustment should be made to the appraisal value to arrive at fair value.

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(Continued)

**SAFE CREDIT UNION**  
**NOTES TO FINANCIAL STATEMENTS**  
**For the Years Ended December 31, 2015 and 2014**

**NOTE 14 - FAIR VALUE** (Continued)

The following table presents quantitative information about Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at December 31, 2015 (in thousands):

<u>Description</u>	<u>Fair Value</u>	<u>Valuation Technique</u>	<u>Significant Unobservable Inputs</u>	<u>Weighted Average</u>
Impaired loans:				
Commercial	\$ 4,309	Appraisal	Comparable sales adjustment	2% to 60%
			Liquidation value adjustment	-46%
Other real estate owned:				
Commercial	\$ 2,361	Appraisal	Comparable sales adjustment	-65% to 56%
Residential real estate	\$ 524	Appraisal	Comparable sales adjustment	-9% to 15%

The following table presents quantitative information about Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at December 31, 2014 (in thousands):

<u>Description</u>	<u>Fair Value</u>	<u>Valuation Technique</u>	<u>Significant Unobservable Inputs</u>	<u>Weighted Average</u>
Impaired loans:				
Commercial	\$ 8,686	Appraisal	Comparable sales adjustment	-7% to 42%
			Liquidation value adjustment	-33%
Other real estate owned:				
Commercial	\$ 3,446	Appraisal	Comparable sales adjustment	-51% to 48%
Residential real estate	\$ 206	Appraisal	Comparable sales adjustment	-11% to 16%