# NORTHWEST FEDERAL CREDIT UNION
# AND SUBSIDIARY

## CONSOLIDATED FINANCIAL STATEMENTS

## YEARS ENDED DECEMBER 31, 2022 AND 2021

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**NORTHWEST FEDERAL CREDIT UNION AND SUBSIDIARY**
**TABLE OF CONTENTS**
**YEARS ENDED DECEMBER 31, 2022 AND 2021**

# INDEPENDENT AUDITORS' REPORT

Supervisory Committee and Board of Directors
Northwest Federal Credit Union and Subsidiary
Herndon, Virginia

## Report on the Audit of the Consolidated Financial Statements

### *Opinion*

We have audited the accompanying consolidated financial statements of Northwest Federal Credit Union and Subsidiary, which comprise the consolidated statements of financial condition as of December 31, 2022 and 2021, and the related consolidated statements of income, comprehensive (loss) income, changes in members' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

In our opinion, based on our audit and the report of the other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Northwest Federal Credit Union and Subsidiary as of December 31, 2022 and 2021, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

We did not audit the financial statements of NW Capital Management, LLC, a wholly owned subsidiary, which statements reflect total assets of approximately $63,622,000 and $63,783,000 as of December 31, 2022 and 2021, and total revenues of approximately $18,847,000 and $20,833,000 for the years then ended, respectively. Those statements were audited by other auditors, whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for NW Capital Management, LLC, is based solely on the report of the other auditors.

### *Basis for Opinion*

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

### *Responsibilities of Management for the Consolidated Financial Statements*

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America, and for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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

### *Auditors' Responsibilities for the Audit of the Consolidated Financial Statements*

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

In performing an audit in accordance with GAAS, we:

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

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

CliftonLarsonAllen LLP

**CliftonLarsonAllen LLP**

Arlington, Virginia
March 28, 2023

## NORTHWEST FEDERAL CREDIT UNION AND SUBSIDIARY
## CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
## DECEMBER 31, 2022 AND 2021
**(IN THOUSANDS)**

| | 2022 | 2021 |
|---|---|---|
| **ASSETS** | | |
| Cash and Cash Equivalents | $ 77,787 | $ 321,775 |
| Deposits in Other Financial Institutions | 2,000 | - |
| Investments: | | |
| Equity Securities | 11,745 | 73,915 |
| Available-for-Sale | 1,013,591 | 1,405,188 |
| Other | 16,749 | 20,138 |
| Loans Held-for-Sale | 2,686 | 113,719 |
| Loans, Net | 2,824,224 | 2,267,062 |
| Accrued Interest Receivable | 9,050 | 7,937 |
| Property and Equipment, Net | 49,086 | 50,447 |
| NCUSIF Deposit | 29,435 | 28,958 |
| Other Assets | 76,418 | 67,373 |
| Total Assets | $ 4,112,771 | $ 4,356,512 |
| **LIABILITIES AND MEMBERS' EQUITY** | | |
| **LIABILITIES** | | |
| Members' Share and Savings Accounts | $ 3,586,578 | $ 3,605,743 |
| Borrowed Funds | 95,000 | 200,000 |
| Accrued Expenses and Other Liabilities | 86,097 | 106,965 |
| Total Liabilities | 3,767,675 | 3,912,708 |
| **MEMBERS' EQUITY** | | |
| Regular Reserves | - | 18,008 |
| Undivided Earnings | 490,599 | 443,619 |
| Accumulated Other Comprehensive Loss | (145,503) | (17,823) |
| Total Member's Equity | 345,096 | 443,804 |
| Total Liabilities and Members' Equity | $ 4,112,771 | $ 4,356,512 |

*See accompanying Notes to Consolidated Financial Statements.*

**NORTHWEST FEDERAL CREDIT UNION AND SUBSIDIARY**
**CONSOLIDATED STATEMENTS OF INCOME**
**YEARS ENDED DECEMBER 31, 2022 AND 2021**
**(IN THOUSANDS)**

| | 2022 | 2021 |
|---|---|---|
| **INTEREST INCOME** | | |
| Loans | $ 98,893 | $ 96,836 |
| Investments and Cash Equivalents | 18,326 | 12,796 |
| Total Interest Income | 117,219 | 109,632 |
| **INTEREST EXPENSE** | | |
| Members' Share and Savings Accounts | 16,852 | 16,665 |
| Borrowed Funds | 3,128 | 3,391 |
| Total Interest Expense | 19,980 | 20,056 |
| Net Interest Income | 97,239 | 89,576 |
| **(CREDIT) PROVISION FOR LOAN LOSSES** | (2,965) | 2,707 |
| Net Interest Income After (Credit) Provision for Loan Losses | 100,204 | 86,869 |
| **NONINTEREST INCOME** | | |
| Fees and Service Charges | 7,391 | 6,002 |
| Interchange Income, Net | 9,724 | 9,636 |
| Gain on Sale of Loans, Net | 865 | 13,557 |
| Gain on Available-for-Sale Investments | - | 456 |
| (Loss) Gain on Equity Securities, Net | (5,546) | 1,174 |
| Other Income | 36,940 | 24,868 |
| Total Noninterest Income | 49,374 | 55,693 |
| **NONINTEREST EXPENSE** | | |
| Employee Compensation and Benefits | 71,698 | 74,444 |
| Operations and Occupancy | 20,893 | 21,248 |
| Advertising and Promotion | 2,000 | 2,201 |
| Loan Servicing | 11,761 | 10,235 |
| Legal and Professional Services | 3,298 | 4,724 |
| Education, Travel, and Officials | 425 | 230 |
| Other Expenses | 10,531 | 9,770 |
| Total Noninterest Expense | 120,606 | 122,852 |
| **NET INCOME** | $ 28,972 | $ 19,710 |

*See accompanying Notes to Consolidated Financial Statements.*

# NORTHWEST FEDERAL CREDIT UNION AND SUBSIDIARY
## CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME
## YEARS ENDED DECEMBER 31, 2022 AND 2021
**(IN THOUSANDS)**

| | 2022 | 2021 |
|---|---|---|
| **NET INCOME** | $ 28,972 | $ 19,710 |
| **OTHER COMPREHENSIVE LOSS** | | |
| Securities Available-for-Sale: | | |
| Unrealized Holding Losses During the Period | (127,680) | (18,245) |
| Reclassification for Gains Included in Net Income | - | (456) |
| Total Other Comprehensive Loss | (127,680) | (18,701) |
| **TOTAL COMPREHENSIVE (LOSS) INCOME** | $ (98,708) | $ 1,009 |

*See accompanying Notes to Consolidated Financial Statements.*

# NORTHWEST FEDERAL CREDIT UNION AND SUBSIDIARY
# CONSOLIDATED STATEMENTS OF CHANGES IN MEMBERS' EQUITY
## YEARS ENDED DECEMBER 31, 2022 AND 2021
**(IN THOUSANDS)**

| | Regular Reserve | Undivided Earnings | Accumulated Other Comprehensive Income (Loss) | Total |
|---|---|---|---|---|
| **BALANCE AT DECEMBER 31, 2020** | $ 18,008 | $ 423,909 | $ 878 | $ 442,795 |
| Net Income | - | 19,710 | - | 19,710 |
| Other Comprehensive Loss | - | - | (18,701) | (18,701) |
| **BALANCE AT DECEMBER 31, 2021** | 18,008 | 443,619 | (17,823) | 443,804 |
| Cumulative Effect of Change in Regulation (See Members' Equity in Note 1) | (18,008) | 18,008 | - | - |
| Net Income | - | 28,972 | - | 28,972 |
| Other Comprehensive Loss | - | - | (127,680) | (127,680) |
| **BALANCE AT DECEMBER 31, 2022** | $ - | $ 490,599 | $ (145,503) | $ 345,096 |

*See accompanying Notes to Consolidated Financial Statements.*

**NORTHWEST FEDERAL CREDIT UNION AND SUBSIDIARY**
**CONSOLIDATED STATEMENTS OF CASH FLOWS**
**YEARS ENDED DECEMBER 31, 2022 AND 2021**
**(IN THOUSANDS)**

| | 2022 | 2021 |
|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | |
| Net Income | $ 28,972 | $ 19,710 |
| Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities: | | |
| (Credit) Provision for Loan Losses | (2,965) | 2,707 |
| Depreciation and Amortization | 5,612 | 6,090 |
| Amortization of Premium on Investment Securities, Net | 3,986 | 4,820 |
| Fair Value Adjustment of Mortgage Servicing Rights | (5,370) | 2,341 |
| Capitalization of Mortgage Servicing Rights | (620) | (4,316) |
| Gain on Sale of Available-for-Sale Investments | - | (456) |
| Net Loss (Gain) on Equity Securities | 5,546 | (1,174) |
| Net Gain on Sale of Loans | (865) | (13,557) |
| Proceeds from Sale of Loans Held-for-Sale | 170,445 | 568,048 |
| Loans Originated for Sale | (58,547) | (546,507) |
| Net Change in: | | |
| Accrued Interest Receivable | (1,113) | 868 |
| Other Assets | (3,055) | (95) |
| Accrued Expenses and Other Liabilities | (20,868) | (4,888) |
| Net Cash Provided by Operating Activities | 121,158 | 33,591 |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | |
| Net Increase in Deposits in Other Financial Institutions | (2,000) | - |
| Purchase of Available-for-Sale Investments | (13,441) | (682,676) |
| Proceeds from Maturities, Sales, and Repayment of Available-for-Sale Investments | 273,372 | 405,041 |
| Purchase of Equity Security Investments | (7,633) | (53,345) |
| Proceeds from Sale of Equity Security Investments | 64,257 | 12,538 |
| Net Change in Other Investments | 3,389 | 3,395 |
| Loan Originations, Net of Principal Collected | (554,197) | (75,135) |
| Increase in NCUSIF Deposit | (477) | (1,318) |
| Purchases of Property and Equipment | (8,374) | (11,713) |
| Proceeds from Disposal of Property and Equipment | 4,123 | 7,747 |
| Net Cash Used by Investing Activities | (240,981) | (395,466) |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | |
| Proceeds from Borrowed Funds | 308,000 | - |
| Payments Made on Borrowed Funds | (413,000) | (50,000) |
| Net Change in Members' Share and Savings Accounts | (19,165) | 180,502 |
| Net Cash (Used) Provided by Financing Activities | (124,165) | 130,502 |
| **NET DECREASE IN CASH AND CASH EQUIVALENTS** | (243,988) | (231,373) |
| Cash and Cash Equivalents - Beginning of Year | 321,775 | 553,148 |
| **CASH AND CASH EQUIVALENTS - END OF YEAR** | $ 77,787 | $ 321,775 |
| **SUPPLEMENTARY DISCLOSURES OF NONCASH AND CASH FLOW INFORMATION** | | |
| Interest Paid on Members' Share and Savings Accounts | $ 16,852 | $ 16,665 |
| Interest Paid on Borrowed Funds | $ 3,128 | $ 3,391 |

*See accompanying Notes to Consolidated Financial Statements.*

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Nature of Operations

Northwest Federal Credit Union (the Credit Union) is a cooperative association holding a corporate charter 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. The principal operations of the Credit Union are located in the Washington, D.C. metropolitan area. Participation in the Credit Union is limited to those individuals that qualify for membership. The field of membership is defined in the Credit Union's Charter and Bylaws.

### Principles of Consolidation

The consolidated financial statements include the accounts of the Credit Union and its wholly owned its subsidiary, NW Capital Management, LLC, a Credit Union Service Organization (CUSO). The CUSO provides insurance and financial services to Credit Union members. All significant intercompany balances and transactions have been eliminated in consolidation.

### Use of Estimates in Preparing Financial Statements

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the valuation of investment securities, and the fair value of mortgage servicing rights.

### Financial Instruments with Concentrations of Credit Risk

The Credit Union may be exposed to credit risk from a regional economic standpoint because a significant concentration of its borrowers work or reside in the Washington D.C. metropolitan area. The Credit Union continually monitors its operations, including the loan and investment portfolios, for potential impairment.

However, the loan portfolio is well diversified, and the Credit Union does not have significant concentrations of credit risk except direct and indirect vehicle and real estate loans which management monitors on an ongoing basis.

### Cash and Cash Equivalents

For the purpose of the consolidated statements of financial condition and the consolidated statements of 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.

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### Deposits in Other Financial Institutions

Deposits in other financial institutions include certificates of deposit. These are stated at cost. The certificates of deposit all mature within two years.

### Securities

Equity securities with readily determinable fair values are reported at fair value with changes in fair value included in noninterest income.

Debt securities are classified as available-for-sale. Securities available-for-sale are carried at fair value with unrealized gains and losses reported in other comprehensive loss. Realized gains and losses on securities available-for-sale are included in other noninterest income and, when applicable, are reported as a reclassification adjustment in other comprehensive loss. Gains and losses on sales of securities are determined using the specific identification method on the trade date. The amortization of premiums and accretion of discounts are recognized in interest income using methods approximating the interest method over the period to maturity. For callable debt securities purchased at a premium, the amortization period is shortened to the earliest call date.

Declines in the fair value of individual available-for-sale debt securities below their cost that are other-than-temporary result in write-downs of the individual securities to their fair value. The Credit Union monitors the investment security portfolio for impairment on an individual security basis and has a process in place to identify securities that could potentially have an impairment that is other-than-temporary. This process involves analyzing the length of time and the extent to which the fair value has been less than the amortized cost basis, the market liquidity for the security, the financial condition and near-term prospects of the issuer, expected cash flows, and the Credit Union's intent and ability to hold the investment for a period of time sufficient to recover the temporary loss. The ability to hold is determined by whether it is more likely than not that the Credit Union will be required to sell the security before its anticipated recovery. A decline in value due to an event that is considered other-than-temporary is recorded as a loss in noninterest income.

The Credit Union did not record any other-than-temporary impairment during the years ended December 31, 2022 and 2021.

### Other Investments

Other investments are carried at cost and are evaluated annually for impairment. In addition, the Credit Union has investments in various Credit Union Service Organizations. These investments are carried, as a practical expedient, at cost, less impairment, plus or minus changes resulting from observable price changes.

### Loans Held-For-Sale

Loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value. Gains and losses on sales of loans are recognized at settlement dates and are determined by the difference between the sales proceeds and the carrying value of the loans. All sales are made without recourse.

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### Loans, Net

The Credit Union grants consumer, residential real estate, and commercial loans to members. In addition, the Credit Union purchases participation loans originated by various other Credit Unions. The ability of the members to honor their contracts is dependent upon the real estate and general economic conditions comprising the Credit Union's field of membership.

Loans that the Credit Union has the intent and ability to hold for the foreseeable future or until maturity or pay-off are stated at their outstanding unpaid principal balances, adjusted for an allowance for loan losses and net deferred origination costs. Interest 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 loans, other than credit card loans, is discontinued at the time the loan is 90 days past due, unless the credit is well-secured and in the process of collection. Consumer loans are typically charged off no later than 180 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 that are 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. 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.

For the year ended December 31, 2022, loan fees and certain direct loan origination costs are deferred, and the net fee or cost is recognized as an adjustment to interest income using methods approximating the interest method over the estimated life of the loans. The Credit Union does not charge commitment fees. For the year ended December 31, 2021, direct loan origination costs are recognized in expense as incurred; however, real estate loan origination points and fees and dealer reserve fees are deferred over the average life of the loan as an adjustment to loan yield.

### Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility 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 collectibility 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.

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### Allowance for Loan Losses (Continued)

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 that amount considered adequate to absorb probable losses in the portfolio based on management's evaluations of the size and current risk characteristics of the loan portfolio. Such evaluations consider prior loss experience, the risk rating distribution of the portfolio, the impact of current internal and external influences on credit loss and the levels of non-performing loans. Specific allowances for loan losses are established for impaired loans on an individual basis. 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. General allowances are established for loans that can be grouped into pools based on similar characteristics. In this process, general allowance factors are based on an analysis of historical charge-off experience (one year) and expected losses given default derived from the Credit Union's internal risk-rating process. These factors are developed and applied to the portfolio in terms of loan type. The qualitative factors associated with the allowances are subjective and require a high degree of management judgment. These factors include the credit quality statistics, recent economic uncertainty, losses incurred from recent events, and lagging data.

A loan is considered impaired when, based on current information and events, it is probable that the Credit Union will be unable to collect the scheduled payments of principal or interest when due, according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### Allowance for Loan Losses (Continued)

Under certain circumstances, the Credit Union will provide borrowers relief through loan restructurings. A restructuring of debt constitutes a troubled debt restructuring (TDR) if the Credit Union for economic or legal reasons related to the borrower's financial difficulties grants a concession to the borrower that it would not otherwise consider. TDR concessions can include reduction of interest rates, extension of maturity dates, forgiveness of principal and/or interest due, or acceptance of other assets in full or partial satisfaction of the debt. The Credit Union considers all aspects of the restructuring to determine whether it has granted a concession to the borrower. An insignificant delay in payment resulting from a restructuring is not deemed to be a concession and would not be considered to be a TDR.

The Credit Union has concluded that TDRs granted during the years ended December 31, 2022 and 2021 were insignificant for the consolidated financial statement disclosure.

The Credit Union maintains a separate general valuation allowance for homogeneous portfolio segments. These portfolio segments and their risk characteristics are described as follows:

**Consumer:** These loans are usually comprised of a large number of small loans. Most loans are made directly for consumer purchases. Economic trends determined by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans.

**Residential Real Estate:** The degree of risk in residential mortgage lending depends primarily on the loan amount in relation to collateral value, the interest rate, and the borrower's ability to repay. These loans generally possess a lower inherent risk of loss than commercial real estate portfolio segments. Economic trends determined by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans.

The portfolio segments that are risk rated and their risk characteristics are described as follows:

**Commercial:** These loans generally possess a higher inherent risk of loss than residential 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 the properties to produce sufficient cash flow to service debt obligations.

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### Allowance for Loan Losses (Continued)

The Credit Union assigns a risk rating to commercial loans and periodically performs detailed internal reviews of all such loans over a certain threshold to identify credit risks and to assess the overall collectibility of the portfolio. These risk ratings are also subject to examination by the Credit Union's regulators. During the internal reviews, management monitors and analyzes the financial condition of borrowers and guarantors, trends in the industries in which the borrowers operate and the fair values of collateral securing the loans. These credit quality indicators are used to assign a risk rating to each individual loan. The risk ratings can be grouped into the following major categories, defined as follows:

**Pass***:* A Pass credit is a loan with no significant existing or known potential credit weaknesses deserving management's close attention.

**Watch List***:* A Watch credit is a loan that otherwise meets the definition of a standard or minimum acceptable quality loan, but which requires more than normal attention due to any of the following items: deterioration of borrower financial condition less severe than those warranting more adverse grading, deterioration of repayment ability and/or collateral value, increased leverage, adverse effects from a downturn in the economy, local or market industry, adverse changes in local or regional employer, management changes (including illness, disability and death) and adverse legal action. Payments are current per the terms of the agreement. If conditions persist or worsen, a more severe risk grade may be warranted.

**Special Mention**: A Special Mention credit is a loan that has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in the deterioration of the repayment prospects for the loan or in the Credit Union's position at some future date. Special Mention credits are not adversely classified and do not expose the Credit Union to sufficient risk to warrant adverse classification.

**Substandard***:* Credits classified as Substandard are loans considered inadequately protected by the current net worth and paying capacity of the borrower or of the collateral pledged, if any. Such loans have a well-defined weakness or weaknesses that jeopardize the repayment 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***:* Credits classified as Doubtful are loans that have all the weaknesses inherent in those classified as Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions and values, highly questionable and improbable.

**Loss***:* Credits classified as Loss are loans considered uncollectible and charged-off.

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### Transfers of Financial Assets

Transfers of financial assets are accounted for as sales only when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) assets have been isolated from the Credit Union, (2) the transferee obtained the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Credit Union does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

The transfer of a participating interest in an entire financial asset must also meet the definition of a participating interest. A participating interest in a financial asset has all of the following characteristics: (1) from the date of transfer, it must represent a proportionate (pro rata) ownership interest in the financial asset, (2) from the date of transfer, all cash flows received, except any cash flows allocated as any compensation for servicing or other services performed, must be divided proportionately among participating interest holders in the amount equal to their share ownership, (3) the rights of each participating interest holder must have the same priority, (4) no party has the right to pledge or exchange the entire financial asset unless all participating interest holders agree to do so.

### Loan Servicing

Servicing assets are recognized separately when servicing rights are acquired through purchase or through sale of financial assets. Servicing rights resulting from the sale or securitization of loans originated by the Credit Union are initially measured at fair value at the date of transfer. The Credit Union measures servicing assets at fair value at each reporting date and reports changes in fair value of servicing assets into noninterest income in the period of which the change occurs.

Fair value is based on market prices for comparable servicing contracts, when available, or alternatively, is based 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. These variables change from quarter to quarter as the market conditions and projected interest rates change and may have an adverse impact on the value of the servicing right and may result in reduction to noninterest income.

### Off-Consolidated Statement of Financial Condition Credit Related Financial Instruments

In the ordinary course of business, the Credit Union has entered into commitments to extend credit. Such financial instruments are recorded when they are funded.

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

**Property and Equipment, Net**

Land and construction in progress are carried at cost. Land includes amounts for grounds improvements depreciated using the straight-line method over an estimated useful life of 20 years. Building, leasehold improvements, and furniture and equipment are carried at cost, less accumulated depreciation and amortization. Buildings and 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 shorter of the useful lives of the assets or the expected terms of the related leases. Expected terms include lease option periods to the extent that the exercise of such options is reasonably assured.

**Leases**

In February 2016, the Financial Accounting Standards Board (FASB) issued ASU 2016-02, *Leases (Topic 842)*. This standard increases transparency and comparability among organizations by requiring the recognition of right-of-use (ROU) assets and lease liabilities on the balance sheet. Most prominent among the changes in the standard is the recognition of ROU assets and lease liabilities by lessees for those leases classified as operating leases. Under the standard, disclosures are required to meet the objective of enabling users of financial statements to assess the amount, timing, and uncertainty of cash flows arising from leases.

The Credit Union adopted the requirements of the guidance effective January 1, 2022 and has elected to apply the provisions of this standard to the beginning of the period of adoption. As such, a ROU asset of $4,960 and a lease liability of $4,960 was recorded as of January 1, 2022.

The Credit Union has elected to adopt the package of practical expedients available in the year of adoption. The Credit Union has elected to adopt the available practical expedient to use hindsight in determining the lease term and in assessing impairment of the Credit Union’s ROU assets.

The Credit Union determines if an arrangement is a lease at inception. Operating leases are included in other assets and accrued expenses and other liabilities in the statements of financial position.

ROU assets represent the Credit Union’s right to use an underlying asset for the lease term and lease liabilities represent the Credit Union’s obligation to make lease payments arising from the lease. ROU assets and liabilities are recognized at the lease commencement date based on the present value of lease payments over the lease term. Lease terms may include options to extend or terminate the lease when it is reasonably certain that the Credit Union will exercise that option. Lease expense for operating lease payments is recognized on a straight-line basis over the lease term. The Credit Union has elected to recognize payments for short-term leases with a lease term of 12 months or less as expense as incurred and these leases are not included as lease liabilities or right of use assets on the statements of financial position.

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### Impairment of Long-Lived Assets

The Credit Union tests long-lived assets for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of carrying amount or fair value less estimated costs to sell.

### NCUSIF Deposit and Share Insurance Premium Assessments

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.

### Members' Share and Savings Accounts

Members' share and savings accounts are subordinated to all other liabilities of the Credit Union upon liquidation. Dividends and interest on members' share and savings accounts, except for interest on certificates of deposit which are set in advance, are based on available earnings at the end of a dividend period and are not guaranteed by the Credit Union. Interest rates on members' share and savings accounts are set by the board of directors, based on an evaluation of current and future market conditions.

### Members' Equity

Prior to January 1, 2022, the Credit Union was required by regulation to maintain a statutory reserve (Regular Reserve). This Regular Reserve, which represented a regulatory restriction on members' equity, was established for the purpose of absorbing losses that exceed undivided earnings and other appropriations of undivided earnings. The Regular Reserve was not available for the payment of interest. Effective January 1, 2022, the Regular Reserve is no longer required by regulation. All Regular Reserve amounts were transferred to Undivided Earnings effective January 1, 2022.

The Credit Union is subject to various regulatory net worth requirements administered by the NCUA.

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### Comprehensive (Loss) 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 consolidated statements of financial condition. Reclassifications from accumulated other comprehensive loss for realized gains (losses) on the sales of available-for-sale investments are reported as noninterest income on the consolidated statements of income.

### Revenue From Contracts with Members

The Credit Union recognizes revenue in accordance with *Revenue from Contracts with Customers (Topic 606).* The Credit Union has elected to use the following optional exemptions that are permitted under the Topic 606, which have been applied consistently to all contracts within all reporting periods presented:

- The Credit Union recognizes the incremental cost of obtaining a contract as an expense, when incurred, if the amortization period of the asset that the Credit Union would have recognized is one year or less.

- For performance obligations satisfied over time, if the Credit Union has a right to consideration from a member in an amount that corresponds directly with the value to the member of the Credit Union's performance completed to date, the Credit Union will generally recognize revenue in the amount to which the Credit Union has a right to invoice.

- The Credit Union does not generally disclose information about its remaining performance obligations for those performance obligations that have an original expected duration of one year or less, or where the Credit Union recognizes revenue in the amount to which the Credit Union has a right to invoice.

Topic 606 does not apply to revenue associated with financial instruments, including revenue from loans and securities. Topic 606 is applicable to noninterest income such as deposit related fees and interchange fees. Significant components of noninterest income considered to be within the scope of Topic 606 are discussed below.

#### *Service Charges on Deposits*

The Credit Union earns fees from its deposit members for transaction-based, account maintenance, and overdraft services. Transaction-based fees, which include services such as ATM use fees, stop payment charges, and ACH fees, are recognized at the time the transaction is executed as that is the point in time the Credit Union fulfills the member's request. Account maintenance fees, which relate primarily to monthly maintenance, are earned over the course of a month, representing the period over which the performance obligation is satisfied. Overdraft fees are recognized at the point in time that the overdraft occurs. Service charges on deposits are withdrawn from the member's account balance.

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### Revenue From Contracts with Members (Continued)

*Interchange Income, Net*

When members use their debit and credit cards to pay merchants for goods or services, the Credit Union retains a fee from the funds collected from the related deposit account and transfers the remaining funds to the payment network for remittance to the merchant. The performance obligation to the merchant is satisfied and the fee is recognized at the point in time when the funds are collected and transferred to the payment network. Interchange fees are recorded net of the related member rewards program costs.

*Investment Advisory Fees*

Revenue from investment advisory and financial planning services are paid by clients three months in advance and deferred and recognized as revenue over the subsequent three months from date of payment. The performance obligation is fulfilled at the end of each month as financial advisors perform their fiduciary responsibilities. Advisory revenues collected prior to when the performance obligation has been fulfilled are recorded as contract liabilities in the consolidated balance sheets.

*Broker-Dealer Referral Fees*

Commission fee revenue from the Company's securities broker-dealer operations consist of referral fees from LPL Financial, LLC and are recorded on a trade-date basis as that is when the performance obligation, which is the purchase or sale of securities to investors, is deemed to have been fulfilled, and normally settled within 30 days.

*Title and Escrow Services*

Revenue generated from the sale of title insurance policies consists of a commission on the sale of the policy as well as loan closing and processing fees, which are recorded upon the loan settlement. The Credit Union acts as a broker between the customer and the underwriter of the title insurance and the Credit Union has no future obligations to the customer. The closing and processing fees are a one-time cost paid by the customer upon settlement of the loan.

### Income Taxes

The Credit Union is exempt, by statute, from federal and state income taxes. The income from the CUSOs, organized as single member LLCs, flows through to the Credit Union, and therefore are not subject to federal and state income taxes.

### Advertising Costs

Advertising costs are expensed as incurred.

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### Retirement Plan

401(k) plan – The Credit Union provides a 401(k) plan, which covers substantially all of the Credit Union's employees who are eligible as to age and length of service. Participants are always 100% vested in the voluntary contributions. The Credit Union may make discretionary matching contributions equal to a uniform percentage of an employee's salary deferral and/or discretionary profit sharing contribution. Credit Union contributions vest at 33% after one year of service, 67% after two years of service and 100% after three years of service. During the years ended December 31, 2022 and 2021, the Credit Union contributed a matching contribution of up to 7% of employee compensation. The Credit Union's contributions to the plan approximated $3,223 and $3,004 for the years ended December 31, 2022 and 2021, respectively.

### Charitable Donation Account (CDA)

In December 2013, the NCUA approved a rule that allows federal credit unions to be able to hold investments within a CDA that are not allowed otherwise, so long as the account is primarily charitable in nature. Among the CDA requirements is a minimum of 51% of the total return from the CDA must be distributed to one or more 501(c)(3) charities. Distributions must also be made to qualified charities no less frequently than every five years. Assets in a CDA also must be held in segregated custodial accounts or special purpose entities regulated by the Office of the Comptroller of the Currency, the Securities and Exchange Commission, or other federal or state financial regulatory agency.

The CDA is made up of several life insurance policies. These totaled $10,513 and $10,229 at December 31, 2022 and 2021, respectively, and are included in other assets on the consolidated statements of financial condition. The policies are carried at the cash surrender value (CSV) of the contract, with changes in the value being recognized in other noninterest income on the consolidated statement of income.

The associated CDA liability is included in accrued expenses and other liabilities and was not considered material at December 31, 2022 and 2021.

### Split Dollar Life Insurance

The Credit Union has made loans for life insurance premium payments to members of top management. The loans are collateralized by the assignment of the policy death benefits and cash values, of each respective life insurance policy. The policies are owned by the executives and the executives have the right to name the beneficiaries for amounts not secured by the assignments. The loans are considered non-recourse and as such, the Credit Union has recorded the balance as the lower of the outstanding loan balance, plus accrued interest, or the cash surrender value of the life insurance policies. The loan balance, including accrued interest, for the arrangements was $8,190 and $8,109 as of December 31, 2022 and 2021, respectively. The associated cash surrender value was $7,598 and $7,378 as of December 31, 2022 and 2021, respectively. The cash surrender value of the plans is included in other assets on the consolidated statements of financial condition. The difference represents the costs to the Credit Union associated with entering into this arrangement.

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### Self-Insured Group Medical Insurance Plan

The Credit Union sponsors a self-insured group medical insurance plan. The plan is designed to provide a specified level of coverage, with stop-loss coverage provided by a commercial insurer in order to limit the Credit Union's exposure. The Credit Union's maximum claim exposure is limited to $150 per person per policy year. Substantially all of the Credit Union employees are enrolled in the plan at December 31, 2022 and 2021. Expenses associated with the plan totaled approximately $5,184 and $5,813 for the years ended December 31, 2022 and 2021, respectively. The Credit Union provides accruals based on the aggregate amount of the liability for reported claims and an estimated liability for claims incurred but not reported. At December 31, 2022 and 2021, Accrued Expenses and Other Liabilities includes an accrued liability related to this plan of $867 and $909, respectively.

### Fair Value Measurements

The Credit Union categorizes its assets and liabilities measured at fair value into a three-level hierarchy based on the priority of the inputs to the valuation technique used to determine fair value. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the inputs used in the determination of the fair value measurement fall within different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement. Assets and liabilities valued at fair value are categorized based on the inputs to the valuation techniques as follows:

*Level 1* – Inputs that utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that the Credit Union has the ability to access.

*Level 2* – Inputs that include quoted prices for similar assets and liabilities in active markets and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument. Fair values for these instruments are estimated using pricing models, quoted prices of securities with similar characteristics, or discounted cash flows.

*Level 3* – Inputs that are unobservable inputs for the asset or liability, which are typically based on an entity's own assumptions, as there is little, if any, related market activity.

Subsequent to initial recognition, the Credit Union may re-measure the carrying value of assets and liabilities measured on a nonrecurring basis to fair value. Adjustments to fair value usually result when certain assets are impaired. Such assets are written down from their carrying amounts to their fair value.

Professional standards allow entities the irrevocable option to elect to measure certain financial instruments and other items at fair value for the initial and subsequent measurement on an instrument-by-instrument basis. The Credit Union adopted the policy to value certain financial instruments at fair value. The Credit Union has not elected to measure any existing financial instruments at fair value; however, it may elect to measure newly acquired financial instruments at fair value in the future.

**(IN THOUSANDS)**

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### New Accounting Pronouncements

In June 2016, the FASB approved ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. In November 2018, the FASB approved ASU 2018-19, *Codification Improvements to Topic 326, Financial Instruments – Credit Losses*. The main objective of the ASUs is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. To achieve this objective, the amendments in the ASUs replace the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. In November 2019, the FASB approved ASU 2019-10, *Financial Instruments – Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842)*. The main objective of this ASU was to delay the effective date for the referenced standards. Based upon the new effective dates instituted by ASU 2019-10, ASU 2016-13 is effective for the Credit Union for the fiscal year and all interim periods beginning after December 15, 2022. Early adoption is permitted for the fiscal year beginning after December 15, 2018, including interim periods within this fiscal year. Management continues to analyze the model to determine the impact of the adoption of ASU 2016-13 on the consolidated financial statements. Management expects the adoption of ASC 2016-13 to significantly increase the Credit Union's allowance for loan losses.

### Subsequent Events

In preparing these consolidated financial statements, the Credit Union has evaluated events and transactions for potential recognition or disclosure through March 28, 2023, the date the consolidated financial statements were available to be issued.

### Reclassification of 2021 Data

Data in the 2021 consolidated financial statements has been reclassified to conform with the presentation of the 2022 consolidated financial statements. This reclassification did not result in any change to consolidated net income or members' equity.

## NOTE 2 SECURITIES AND OTHER INVESTMENTS

### Equity Securities

Equity securities are comprised of exchange traded funds and mutual fund investments. Such investments are recorded at fair value with changes in fair value reflected in income on investment securities. The fair values of equity securities as of December 31 are as follows:

| | 2022 | 2021 |
|---|---|---|
| Exchange-Traded Funds | $ 300 | $ 7,241 |
| Mutual Funds | 11,445 | 66,674 |
| Total | $ 11,745 | $ 73,915 |

(IN THOUSANDS)

## NOTE 2 SECURITIES AND OTHER INVESTMENTS (CONTINUED)

### Equity Securities

The following table shows a reconciliation of realized and unrealized (losses) gains for the years ended December 31:

| | 2022 | 2021 |
|---|---|---|
| Net (Loss) Gain Recognized During the Year on Equity Securities | $ (5,546) | $ 1,174 |
| Less: Net Realized Losses on Sales of Equity Securities | 4,110 | 219 |
| Unrealized (Losses) Gains Recognized During the Reporting Period on Equity Securities Still Held as of December 31 | $ (1,436) | $ 1,393 |

### Available-for-Sale Investments

Investments classified as available-for-sale consist of the following:

| | December 31, 2022 | | | |
|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| U.S. Government Obligations and Federal Agencies Securities | $ 43,644 | $ 24 | $ (2,175) | $ 41,493 |
| SBA Loan Pools | 22,313 | - | (570) | 21,743 |
| Mortgage-Backed Securities | 1,057,013 | - | (141,215) | 915,798 |
| Municipal Bonds | 17,920 | - | (682) | 17,238 |
| Corporate Bonds | 18,204 | - | (885) | 17,319 |
| Total | $ 1,159,094 | $ 24 | $ (145,527) | $ 1,013,591 |

| | December 31, 2021 | | | |
|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| U.S. Government Obligations and Federal Agencies Securities | $ 43,649 | $ 60 | $ (352) | $ 43,357 |
| SBA Loan Pools | 35,072 | 8 | (1,038) | 34,042 |
| Mortgage-Backed Securities | 1,305,593 | 2,172 | (19,003) | 1,288,762 |
| Municipal Bonds | 24,269 | 3 | (74) | 24,198 |
| Corporate Bonds | 14,428 | 416 | (15) | 14,829 |
| Total | $ 1,423,011 | $ 2,659 | $ (20,482) | $ 1,405,188 |

There were no sales of securities available for sale during the year ended December 31, 2022. Sales of securities available-for-sale resulted in gross gains of approximately $456 and gross losses of approximately $-0- during the year ended December 31, 2021.

(IN THOUSANDS)

## NOTE 2 SECURITIES AND OTHER INVESTMENTS (CONTINUED)

**Available-for-Sale Investments (Continued)**

At December 31, 2021, securities carried at approximately $1,143,367 were pledged as collateral to secure borrowed funds with the FHLB. There were no securities pledged at December 31, 2022.

The Credit Union is generally restricted from investing in certain security types as defined in the NCUA Rules and Regulations under 12 CFR Sec 703. The Credit Union has invested in otherwise non-permissible securities for the purposes of benefit prefunding and charitable contributions in accordance with 12 CFR Sec 701.19(c) and Sec 721.3(2). All investments in mutual funds, equity securities, municipal bonds, and corporate bonds were acquired for the purposes of benefit prefunding and charitable contributions.

The amortized cost and fair value of securities available-for-sale at December 31, 2022 by contractual maturity are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

| | Amortized Cost | Estimated Fair Value |
|---|---|---|
| U.S. Government Obligations and Federal Agency Securities, Municipal Bonds and Corporate Bonds: | | |
| Less than 1 Year Maturity | $ 24,798 | $ 24,192 |
| 1 - 5 Years Maturity | 54,970 | 51,858 |
| Subtotal | 79,768 | 76,050 |
| SBA Loan Pools | 22,313 | 21,743 |
| Mortgage-Backed Securities | 1,057,013 | 915,798 |
| Total | $ 1,159,094 | $ 1,013,591 |

(IN THOUSANDS)

## NOTE 2 SECURITIES AND OTHER INVESTMENTS (CONTINUED)

### Available-for-Sale Investments (Continued)

Information pertaining to investments with gross unrealized losses at December 31, 2022 and 2021, aggregated by investment category and length of time that the investments have been in a continuous loss position, is as follows:

| | Less Than Twelve Months | | Greater Than Twelve Months | | |
|---|---|---|---|---|---|
| | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Total Unrealized Losses |
| **2022** | | | | | |
| U.S. Government Obligations and Federal Agencies Securities | $ - | $ - | $ (2,175) | $ 31,469 | $ (2,175) |
| SBA Loan Pools | (10) | 3,127 | (560) | 18,616 | (570) |
| Mortgage-Backed Securities | (7,498) | 188,583 | (133,717) | 727,215 | (141,215) |
| Municipal Bonds | (157) | 3,958 | (525) | 13,280 | (682) |
| Corporate Bonds | (520) | 10,651 | (365) | 6,668 | (885) |
| Total | $ (8,185) | $ 206,319 | $ (137,342) | $ 797,248 | $ (145,527) |
| **2021** | | | | | |
| U.S. Government Obligations and Federal Agencies Securities | $ (352) | $ 33,297 | $ - | $ - | $ (352) |
| SBA Loan Pools | (1,038) | 33,177 | - | - | (1,038) |
| Mortgage-Backed Securities | (19,003) | 1,026,467 | - | - | (19,003) |
| Municipal Bonds | (74) | 18,107 | - | - | (74) |
| Corporate Bonds | (15) | 6,127 | - | - | (15) |
| Total | $ (20,482) | $ 1,117,175 | $ - | $ - | $ (20,482) |

At December 31, 2022, the 628 securities with unrealized losses have depreciated 12.7% from the Credit Union's amortized cost basis. These unrealized losses are a result of expected fluctuations in the markets and relate principally to current interest rates for similar types of securities. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and industry analysts' reports. As management has the intent and ability to hold securities until maturity or for the foreseeable future for those classified as available for sale, no declines are deemed to be other-than-temporary.

In general, investments are exposed to various risks, such as interest rate, credit, and overall market volatility risk. Due to the level of risk associated with certain investments, it is reasonably possible that changes in the values of the investments will occur in the near term and that such changes could be material.

(IN THOUSANDS)

## NOTE 2 SECURITIES AND OTHER INVESTMENTS (CONTINUED)

**Other Investments**

Other investments at December 31 are summarized as follows:

| | 2022 | 2021 |
|---|---|---|
| Investments in CUSOs | $ 799 | $ 1,549 |
| FHLB Stock | 6,001 | 9,615 |
| Central Liquidity Facility Stock | 9,949 | 8,974 |
| Total | $ 16,749 | $ 20,138 |

*Investments in CUSOs*

The Credit Union has noncontrolling equity ownership interest in other credit union service organizations (CUSOs). As a practical expedient, such investments are carried at cost, less impairment, plus or minus changes resulting from observable price changes.

*FHLB Stock*

The Credit Union has an investment in Federal Home Loan Bank (FHLB) stock that allows the Credit Union access to other FHLB financial services. The stock qualifies as a restricted stock and as such is not subject to investment security accounting treatment and is therefore reported at cost, subject to impairment.

*Central Liquidity Facility Stock*

The Credit Union is a member of the NCUA Central Liquidity Facility (Facility), which was formed to assist member credit unions in meeting their short-term liquidity needs. Membership is obtained through investment in shares of the Facility as determined by a statutory formula. As of December 31, 2022 and 2021, the Credit Union had not borrowed from the Facility.

(IN THOUSANDS)

## NOTE 3 LOANS, NET

Loans, net consisted of the following at December 31:

| | 2022 | 2021 |
|---|---|---|
| Consumer: | | |
| New Indirect | $ 630,143 | $ 557,704 |
| Used Indirect | 741,059 | 463,629 |
| New Vehicle | 83,191 | 77,705 |
| Used Vehicle | 163,441 | 152,054 |
| Unsecured | 50,191 | 53,450 |
| Credit Cards | 73,716 | 72,987 |
| Other Secured | 2,221 | 2,023 |
| Total Consumer | 1,743,962 | 1,379,552 |
| Residential Real Estate: | | |
| First Mortgages | 796,050 | 620,017 |
| Second Mortgages | 76,535 | 37,102 |
| Home Equity | 109,623 | 89,050 |
| Total Residential Real Estate | 982,208 | 746,169 |
| Commercial: | | |
| Real Estate | 37,155 | 47,686 |
| Other | 35,071 | 81,343 |
| Purchased Participations | 7,985 | 10,755 |
| Total Commercial | 80,211 | 139,784 |
| Total Loans | 2,806,381 | 2,265,505 |
| Deferred Loan Costs (Fees) | 26,219 | 14,832 |
| Allowance for Loan Losses | (8,376) | (13,275) |
| Loans, Net | $ 2,824,224 | $ 2,267,062 |

The Credit Union has purchased loan participations originated by various other financial institutions which are secured by commercial property and real estate. These loan participations were purchased without recourse and the originating financial institutions perform all loan servicing functions on these loans. The total purchased participation loans are included in the Purchased Participations segment above.

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act (the Act) was signed to provide emergency assistance and health care response for individuals, families and businesses affected by the coronavirus pandemic. The Small Business Administration (SBA) received funding and authority through the Act to modify existing loan programs and establish a new loan program to assist small businesses nationwide adversely impacted by the COVID-19 emergency. Section 1102 of the Act temporarily permits SBA to guarantee 100 percent of 7(a) loans under a new program titled the “Paycheck Protection Program (PPP).” Section 1106 of the Act provides for forgiveness of up to the full principal amount of qualifying loans under the PPP. As of December 31, 2022 and 2021 outstanding SBA PPP balances were $8,805 and $47,803, which are included in Other business loans.

(IN THOUSANDS)

## NOTE 3 LOANS, NET (CONTINUED)

Specific changes in the allowance for loan losses and recorded investment in loans by segment are as follows:

| | Consumer | Residential Real Estate | Commercial | Total |
|---|---|---|---|---|
| **December 31, 2022** | | | | |
| ***Allowance for Loan Losses:*** | | | | |
| Beginning Balance | $ 11,313 | $ 703 | $ 1,259 | $ 13,275 |
| Credit for Loan Losses | (1,906) | (420) | (639) | (2,965) |
| Charge-offs | (4,533) | - | (335) | (4,868) |
| Recoveries | 2,602 | 232 | 100 | 2,934 |
| **Ending Balance** | $ 7,476 | $ 515 | $ 385 | $ 8,376 |
| Ending Balance: Individually Evaluated for Impairment | $ 143 | $ - | $ 220 | $ 363 |
| Ending Balance: Collectively Evaluated for Impairment | 7,333 | 515 | 165 | 8,013 |
| **Ending Balance** | $ 7,476 | $ 515 | $ 385 | $ 8,376 |
| ***Loans:*** | | | | |
| Ending Balance: Individually Evaluated for Impairment | $ 581 | $ 2,814 | $ 1,112 | $ 4,507 |
| Ending Balance: Collectively Evaluated for Impairment | 1,743,381 | 979,394 | 79,099 | 2,801,874 |
| **Ending Balance** | $ 1,743,962 | $ 982,208 | $ 80,211 | $ 2,806,381 |

| | Consumer | Residential Real Estate | Commercial | Total |
|---|---|---|---|---|
| **December 31, 2021** | | | | |
| ***Allowance for Loan Losses:*** | | | | |
| Beginning Balance | $ 13,147 | $ 1,279 | $ 618 | $ 15,044 |
| Provision (Credit) for Loan Losses | 2,506 | (444) | 645 | 2,707 |
| Charge-offs | (6,872) | (322) | (161) | (7,355) |
| Recoveries | 2,532 | 190 | 157 | 2,879 |
| **Ending Balance** | $ 11,313 | $ 703 | $ 1,259 | $ 13,275 |
| Ending Balance: Individually Evaluated for Impairment | $ 116 | $ - | $ 921 | $ 1,037 |
| Ending Balance: Collectively Evaluated for Impairment | 11,197 | 703 | 338 | 12,238 |
| **Ending Balance** | $ 11,313 | $ 703 | $ 1,259 | $ 13,275 |
| ***Loans:*** | | | | |
| Ending Balance: Individually Evaluated for Impairment | $ 753 | $ 3,705 | $ 3,655 | $ 8,113 |
| Ending Balance: Collectively Evaluated for Impairment | 1,378,799 | 742,464 | 136,129 | 2,257,392 |
| **Ending Balance** | $ 1,379,552 | $ 746,169 | $ 139,784 | $ 2,265,505 |

**(IN THOUSANDS)**

## NOTE 3 LOANS, NET (CONTINUED)

Commercial Credit Quality Indicators: As part of the on-going monitoring of the credit quality of the Credit Union's commercial loan portfolio, management tracks certain credit quality indicators including trends related to the risk ratings of commercial loans; the level of classified loans; net charge-offs; nonperforming loans; and the general economic conditions in the market area.

The following tables show the commercial loan portfolio segments allocated by management's internally assigned risk ratings:

| | Real Estate | Other | Purchased Participations | Total |
|---|---|---|---|---|
| **December 31, 2022** | | | | |
| Pass | $ 31,736 | $ 26,724 | $ 1,250 | $ 59,710 |
| Watch List | - | - | 3,009 | 3,009 |
| Special Mention | 5,419 | 8,347 | 3,081 | 16,847 |
| Doubtful | - | - | 645 | 645 |
| Total | $ 37,155 | $ 35,071 | $ 7,985 | $ 80,211 |
| **December 31, 2021** | | | | |
| Pass | $ 40,654 | $ 81,297 | $ 1,761 | $ 123,712 |
| Watch List | - | - | 4,496 | 4,496 |
| Special Mention | 3,647 | 46 | 3,857 | 7,550 |
| Substandard | - | - | 641 | 641 |
| Doubtful | 2,794 | - | - | 2,794 |
| Loss | 591 | - | - | 591 |
| Total | $ 47,686 | $ 81,343 | $ 10,755 | $ 139,784 |

**(IN THOUSANDS)**

## NOTE 3 LOANS, NET (CONTINUED)

The following tables show the classes within the Residential Real Estate and Consumer portfolio segments allocated by credit quality. Management tracks loan performance. When a loan becomes 90 days past due, it is classified as a nonperforming loan.

| **December 31, 2022** | Performing | Nonperforming | Total |
|---|---|---|---|
| Consumer: | | | |
| New Indirect | $ 629,509 | $ 634 | $ 630,143 |
| Used Indirect | 739,958 | 1,101 | 741,059 |
| New Vehicle | 83,164 | 27 | 83,191 |
| Used Vehicle | 163,314 | 127 | 163,441 |
| Unsecured | 50,016 | 175 | 50,191 |
| Credit Cards | 73,423 | 293 | 73,716 |
| Other Secured | 2,221 | - | 2,221 |
| Total Consumer | $ 1,741,605 | $ 2,357 | $ 1,743,962 |
| Residential Real Estate: | | | |
| First Mortgages | $ 794,295 | $ 1,755 | $ 796,050 |
| Second Mortgages | 76,417 | 118 | 76,535 |
| Home Equity | 109,423 | 200 | 109,623 |
| Total Residential Real Estate | $ 980,135 | $ 2,073 | $ 982,208 |

| **December 31, 2021** | Performing | Nonperforming | Total |
|---|---|---|---|
| Consumer: | | | |
| New Indirect | $ 556,102 | $ 1,602 | $ 557,704 |
| Used Indirect | 462,509 | 1,120 | 463,629 |
| New Vehicle | 77,640 | 65 | 77,705 |
| Used Vehicle | 151,876 | 178 | 152,054 |
| Unsecured | 53,182 | 268 | 53,450 |
| Credit Cards | 72,987 | - | 72,987 |
| Other Secured | 2,023 | - | 2,023 |
| Total consumer | $ 1,376,319 | $ 3,233 | $ 1,379,552 |
| Residential Real Estate: | | | |
| First Mortgages | $ 618,178 | $ 1,839 | $ 620,017 |
| Second Mortgages | 36,982 | 120 | 37,102 |
| Home Equity | 88,560 | 490 | 89,050 |
| Total Residential Real Estate | $ 743,720 | $ 2,449 | $ 746,169 |

**(IN THOUSANDS)**

## NOTE 3 LOANS, NET (CONTINUED)

Information concerning impaired loans as of December 31, 2022 and 2021 is as follows:

| **December 31, 2022** | Unpaid Principal Balance | Related Allowance | Average Recorded Investment |
|---|---|---|---|
| ***With No Specific Reserve Recorded:*** | | | |
| Consumer: | | | |
| New Indirect | $ 185 | $ - | $ 194 |
| Used Indirect | 36 | - | 91 |
| Used Vehicle | 60 | - | 68 |
| Unsecured | - | - | 39 |
| Residential Real Estate: | | | |
| First Mortgages | 2,433 | - | 2,645 |
| Second Mortgages | 246 | - | 260 |
| Home Equity | 135 | - | 355 |
| Commercial: | | | |
| Real Estate | 60 | - | 1,354 |
| Purchased Participations | - | - | 16 |
| Subtotal | 3,155 | - | 5,022 |
| ***With Specific Reserve Recorded:*** | | | |
| Consumer: | | | |
| New Indirect | 122 | 22 | 144 |
| Used Indirect | 7 | 2 | 4 |
| Used Vehicle | 113 | 61 | 57 |
| Unsecured | 58 | 58 | 72 |
| Commercial: | | | |
| Real Estate | 1,052 | 220 | 946 |
| Other | - | - | 68 |
| Subtotal | 1,352 | 363 | 1,291 |
| **Total by Segment** | | | |
| Consumer | $ 581 | $ 143 | $ 669 |
| Residential Real Estate | 2,814 | - | 3,260 |
| Commercial | 1,112 | 220 | 2,384 |
| Total | $ 4,507 | $ 363 | $ 6,313 |

**(IN THOUSANDS)**

## NOTE 3 LOANS, NET (CONTINUED)

| **December 31, 2021** | Unpaid Principal Balance | Related Allowance | Average Recorded Investment |
|---|---|---|---|
| ***With No Specific Reserve Recorded:*** | | | |
| Consumer: | | | |
| New Indirect | $ 202 | $ - | $ 101 |
| Used Indirect | 145 | - | 73 |
| Used Vehicle | 76 | - | 62 |
| Unsecured | 78 | - | 79 |
| Residential Real Estate: | | | |
| First Mortgages | 2,857 | - | 3,282 |
| Second Mortgages | 273 | - | 254 |
| Home Equity | 575 | - | 469 |
| Commercial: | | | |
| Real Estate | 2,648 | - | 1,324 |
| Purchased Participations | 32 | - | 39 |
| Subtotal | 6,886 | - | 5,683 |
| ***With Specific Reserve Recorded:*** | | | |
| Consumer: | | | |
| New Indirect | 166 | 30 | 235 |
| Unsecured | 86 | 86 | 88 |
| Commercial: | | | |
| Real Estate | 839 | 785 | 550 |
| Other | 136 | 136 | 47 |
| Subtotal | 1,227 | 1,037 | 920 |
| **Total by Segment** | | | |
| Consumer | $ 753 | $ 116 | $ 638 |
| Residential Real Estate | 3,705 | - | 4,005 |
| Commercial | 3,655 | 921 | 1,960 |
| Total | $ 8,113 | $ 1,037 | $ 6,603 |

Interest income recognized on impaired loans was not significant during the years ended December 31, 2022 and 2021. In addition, the recorded investment approximates the unpaid principal balance as of December 31, 2022 and 2021.

(IN THOUSANDS)

## NOTE 3 LOANS, NET (CONTINUED)

The following tables show an aging analysis of the loan portfolio by time past due:

| | Accruing Interest | | | Nonaccrual | |
|---|---|---|---|---|---|
| December 31, 2022 | Current | 30-59 Days | 60-89 Days | Greater Than 90 Days | Total Loans |
| Consumer: | | | | | |
| New Indirect | $ 623,922 | $ 4,825 | $ 762 | $ 634 | $ 630,143 |
| Used Indirect | 733,936 | 4,870 | 1,152 | 1,101 | 741,059 |
| New Vehicle | 83,027 | 121 | 16 | 27 | 83,191 |
| Used Vehicle | 162,891 | 405 | 18 | 127 | 163,441 |
| Unsecured | 49,326 | 397 | 293 | 175 | 50,191 |
| Credit Cards | 72,922 | 354 | 147 | 293 | 73,716 |
| Other Secured | 2,215 | 6 | - | - | 2,221 |
| Total Consumer | 1,728,239 | 10,978 | 2,388 | 2,357 | 1,743,962 |
| Residential Real Estate: | | | | | |
| First Mortgages | 791,729 | 1,795 | 771 | 1,755 | 796,050 |
| Second Mortgages | 76,344 | 73 | - | 118 | 76,535 |
| Home Equity | 108,944 | 397 | 82 | 200 | 109,623 |
| Total Residential Real Estate | 977,017 | 2,265 | 853 | 2,073 | 982,208 |
| Commercial: | | | | | |
| Real Estate | 34,371 | 2,784 | - | - | 37,155 |
| Other | 35,028 | - | 43 | - | 35,071 |
| Purchased Participations | 7,843 | - | 142 | - | 7,985 |
| Total Commercial | 77,242 | 2,784 | 185 | - | 80,211 |
| Total | $ 2,782,498 | $ 16,027 | $ 3,426 | $ 4,430 | $ 2,806,381 |

| | Accruing Interest | | | Nonaccrual | |
|---|---|---|---|---|---|
| December 31, 2021 | Current | 30-59 Days | 60-89 Days | Greater Than 90 Days | Total Loans |
| Consumer: | | | | | |
| New Indirect | $ 549,019 | $ 5,436 | $ 1,647 | $ 1,602 | $ 557,704 |
| Used Indirect | 456,236 | 4,758 | 1,515 | 1,120 | 463,629 |
| New Vehicle | 77,449 | 151 | 40 | 65 | 77,705 |
| Used Vehicle | 151,299 | 423 | 154 | 178 | 152,054 |
| Unsecured | 52,412 | 520 | 250 | 268 | 53,450 |
| Credit Cards | 72,337 | 467 | 183 | - | 72,987 |
| Other Secured | 2,023 | - | - | - | 2,023 |
| Total Consumer | 1,360,775 | 11,755 | 3,789 | 3,233 | 1,379,552 |
| Residential Real Estate: | | | | | |
| First Mortgages | 615,863 | 854 | 1,461 | 1,839 | 620,017 |
| Second Mortgages | 36,908 | 63 | 11 | 120 | 37,102 |
| Home Equity | 88,155 | 116 | 289 | 490 | 89,050 |
| Total Residential Real Estate | 740,926 | 1,033 | 1,761 | 2,449 | 746,169 |
| Commercial: | | | | | |
| Real Estate | 47,667 | - | - | 19 | 47,686 |
| Other | 77,958 | - | - | 3,385 | 81,343 |
| Purchased Participations | 10,755 | - | - | - | 10,755 |
| Total Commercial | 136,380 | - | - | 3,404 | 139,784 |
| Total | $ 2,238,081 | $ 12,788 | $ 5,550 | $ 9,086 | $ 2,265,505 |

**(IN THOUSANDS)**

## NOTE 4 LOAN SERVICING

Loans serviced for others are not included in the accompanying consolidated statements of financial condition. The unpaid principal balance of loans serviced for others were $1,440,018 and $1,569,511 as of December 31, 2022 and 2021, respectively.

Custodial funds in escrow represent member payments for principal and interest, as well as for taxes and insurance. These amounts are held in escrow, with a corresponding liability recorded until the date that such funds are released by the Credit Union for their intended purpose. As of December 31, 2022 and 2021, the Credit Union held $5,377 and $6,690, respectively, in escrow related to the loans serviced for FNMA.

The fair value of mortgage servicing rights was determined using discount rates of 7.90% and 8.48% and average prepayment speeds of 4.40% and 15.63% for the years ended December 31, 2022 and 2021, respectively.

A summary of the changes in the balance of mortgage servicing rights included in other assets in the consolidated statements of financial condition in 2022 and 2021 are as follows:

| | 2022 | 2021 |
|---|---|---|
| Balance, Beginning of Year | $ 11,848 | $ 9,873 |
| Servicing Assets Capitalized | 620 | 4,316 |
| Fair Value Adjustment | 5,370 | (2,341) |
| Balance, End of Year | $ 17,838 | $ 11,848 |

## NOTE 5 PROPERTY AND EQUIPMENT, NET

Property and equipment, net at December 31 is summarized as follows:

| | 2022 | 2021 |
|---|---|---|
| Land | $ 17,447 | $ 17,447 |
| Buildings | 40,560 | 40,560 |
| Leasehold Improvements | 20,373 | 19,439 |
| Computer Equipment | 27,694 | 24,633 |
| Furniture and Equipment | 6,457 | 6,179 |
| Subtotal | 112,531 | 108,258 |
| Accumulated Depreciation and Amortization | (63,445) | (57,811) |
| Total | $ 49,086 | $ 50,447 |

The Credit Union has leased office space at its main office location under a noncancellable operating lease. Rental income under the operating leases, included in noninterest income, were $1,688 and $1,370 for the years ended December 31, 2022 and 2021, respectively.

**(IN THOUSANDS)**

## NOTE 6 MEMBERS' SHARE AND SAVINGS ACCOUNTS

Members' share and savings accounts at December 31 are summarized as follows:

| | 2022 | 2021 |
|---|---|---|
| Share Draft Accounts | $ 778,328 | $ 834,755 |
| Shares and Equivalents | 840,208 | 851,563 |
| Money Market Accounts | 1,182,223 | 1,278,357 |
| Individual Retirement Accounts (IRA) Shares | 58,194 | 61,035 |
| Share and IRA Certificates of Deposit | 727,625 | 580,033 |
| Total | $ 3,586,578 | $ 3,605,743 |

Share and IRA certificates by maturity are summarized as follows:

| | 2022 |
|---|---|
| 0 - 1 Year | $ 460,403 |
| 1 - 2 Years | 135,144 |
| 2 - 3 Years | 90,389 |
| 3 - 4 Years | 14,881 |
| 4 - 5 Years | 26,808 |
| Total | $ 727,625 |

The NCUSIF insures members' accounts and individual retirement accounts up to $250.

The aggregate amount of certificates of deposit in denominations of $250 or more was $240,560 and $166,324 at December 31, 2022 and 2021, respectively.

## NOTE 7 BORROWED FUNDS

As of December 31, 2022 and 2021, in aggregate, the Credit Union maintained $175,000 and $75,000, respectively, in unsecured and secured line of credit agreements with various institutions, and are secured by a blanket security interest in the Credit Union's investment and loan portfolio. No amounts were outstanding on these line of credit agreements as of December 31, 2022 and 2021.

The Credit Union has entered into an agreement with the Federal Reserve Bank of Richmond that allows the Credit Union to obtain advances and to pledge and grant a security interest in the Credit Union's assets to a Federal Reserve Bank. Borrowings are secured by indirect vehicle loans totaling approximately $862,418. As of December 31, 2022, the Credit Union has advanced $5,000 under the terms of this agreement. The note carries a fixed interest rate of 4.50%. There were no amounts outstanding under this agreement as of December 31, 2021.

**(IN THOUSANDS)**

## NOTE 7 BORROWED FUNDS (CONTINUED)

As of December 31, 2022 and 2021, the Credit Union had access to a pre-approved line of credit for $954,912 and $879,007, respectively, from the FHLB, secured by specific mortgage loans and investment securities totaling approximately $1,044,912 and $1,079,007, respectively. As of December 31, 2022 and 2021, the Credit Union has advanced $90,000 and $200,000, respectively, under the terms of this agreement. The notes carry adjustable interest rates between 4.39% and 4.66%. In addition, some of the advances are convertible and may be required to be repaid at predetermined dates prior to the stated maturity date of the advance.

The notes mature as follows:

| Year Ending December 31, | 2022 |
|---|---|
| 2024 | $ 55,000 |
| 2025 | 25,000 |
| 2026 | 15,000 |
| Total | $ 95,000 |

## NOTE 8 LEASES

The Credit Union leases eight branch facilities under noncancelable operating leases and is required to pay increases in real estate taxes on these facilities in addition to the minimum rents. Total rental expense for both noncancelable and cancelable operating leases included in office and occupancy expenses was approximately $1,011 and $1,068 for the years ended December 31, 2022 and 2021, respectively.

Minimum future lease payments by year under noncancelable operating leases is as follows:

| Year Ending December 31, | Amount |
|---|---|
| 2023 | $ 955 |
| 2024 | 748 |
| 2025 | 520 |
| 2026 | 441 |
| 2027 | 452 |
| Thereafter | 1,165 |
| Total Undiscounted Lease Payments | 4,281 |
| Less Imputed Interest | (352) |
| Total Right of Use Assets and Lease Liabilities | $ 3,929 |

Right of use lease assets and lease liabilities were calculated using a weighted average discount rate (incremental borrowing rate) ranging from 0.57% to 1.91% at December 31, 2022.

(IN THOUSANDS)

## NOTE 9 COMMITMENTS AND CONTINGENT LIABILITIES

**Off-Consolidated Statement of Financial Condition 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 consolidated 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 consolidated financial statements.

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. Collateral held varies but may include consumer assets, residential real estate, and member share balances.

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.

Unfunded loan commitments at December 31 are summarized as follows:

| | 2022 | 2021 |
|---|---|---|
| Credit Card | $ 295,057 | $ 292,387 |
| Commercial | 17,808 | - |
| Home Equity | 171,225 | 136,791 |
| Overdraft Protection | 26,752 | 25,034 |
| Other Consumer | 41,620 | 58,814 |
| Total | $ 552,462 | $ 513,026 |

At December 31, 2022 and 2021, the Credit Union had first mortgage loans in the amount of $8,919 and $44,784, respectively, which had been approved but not yet disbursed.

**Legal Contingencies**

The Credit Union is a 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.

(IN THOUSANDS)

## NOTE 10 REGULATORY NET WORTH REQUIREMENTS

Quantitative measures established by regulation to ensure capital adequacy require the Credit Union to maintain minimum ratios (set forth in the table following) of net worth to total assets (as defined by the regulation). Effective December 31, 2021, and earlier, credit unions were also required to calculate a Risk-Based Net Worth Requirement (RBNWR) which established whether or not the Credit Union will be considered "complex" under the regulatory framework. The minimum ratio to be considered complex under the regulatory framework was 6.00%.

Effective in 2022, the NCUA adopted the risk-based capital calculation which applies only to federally insured, natural person credit unions with quarter-end total assets exceeding $500 million who do not qualify for, or opt into, the complex credit union leverage ratio (CCULR) framework described in §702.104(d).

As of December 31, 2022, the most recent call reporting period, the NCUA categorized the Credit Union initially 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% of assets. In addition, the credit union, if complex, must maintain a minimum risk-based capital ratio of 10% or greater. There are no conditions or events since that notification that management believes have changed the institution's category.

The Credit Union's actual capital amounts and ratios are also presented in the table following.

| | Actual | | To be Adequately Capitalized Under Prompt Corrective Action Provision | | To be Well Capitalized Under Prompt Corrective Action Provision | |
|---|---|---|---|---|---|---|
| | Amount | Ratio | Amount | Ratio | Amount | Ratio |
| December 31, 2022 | | | | | | |
| Net Worth | $ 490,599 | 11.93% | $ 246,766 | 6.00% | $ 287,894 | 7.00% |
| Risk-Based Capital Ratio | $ 461,467 | 19.18% | $ 192,463 | 8.00% | $ 240,578 | 10.00% |
| December 31, 2021 | | | | | | |
| Net Worth | $ 461,627 | 10.60% | $ 261,391 | 6.00% | $ 304,956 | 7.00% |
| Risk-Based Net Worth Requirement | $ 258,777 | 5.94% | N/A | N/A | N/A | N/A |

Because the net worth and risk-based capital ratios exceed the well capitalized thresholds, the Credit Union retains its original category.

**(IN THOUSANDS)**

## NOTE 11 RELATED-PARTY TRANSACTIONS

The majority of employees and all members of the Board of Directors and the Supervisory Committee have member accounts at the Credit Union, including share, deposit and loan accounts. The terms of transactions involving these accounts, such as interest and dividend rates, are comparable to other members.

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, 2022 and 2021 are $15,160 and $15,604, respectively. The aggregate principal advances and principal repayments are not significant.

Deposits from the Credit Union's board of directors, committee members, and senior executive staff held by the Credit Union as of December 31, 2022 and 2021 are not significant.

## NOTE 12 FAIR VALUE OF FINANCIAL INSTRUMENTS

### Recurring Basis

The Credit Union uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. For additional information on how the Credit Union measures fair value refer to Note 1 – Summary of Significant Accounting Policies. The following tables present the balances of the assets and liabilities measured at fair value on a recurring basis:

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total |
|---|---|---|---|---|
| **December 31, 2022** | | | | |
| Equity Securities | $ 11,745 | $ - | $ - | $ 11,745 |
| Available-for-Sale | - | 1,013,591 | - | 1,013,591 |
| Mortgage Servicing Rights | - | - | 17,838 | 17,838 |
| Total | $ 11,745 | $ 1,013,591 | $ 17,838 | $ 1,043,174 |
| **December 31, 2021** | | | | |
| Equity Securities | $ 73,915 | $ - | $ - | $ 73,915 |
| Available-for-Sale | - | 1,405,188 | - | 1,405,188 |
| Mortgage Servicing Rights | - | - | 11,848 | 11,848 |
| Total | $ 73,915 | $ 1,405,188 | $ 11,848 | $ 1,490,951 |

## NOTE 12 FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

### Recurring Basis (Continued)

*Securities – Equity and Available for Sale*

When available, the Credit Union uses quoted market prices to determine the fair value of securities; such items are classified in Level 1 of the fair value hierarchy. For the Credit Union's securities where quoted prices are not available for identical securities in an active market, the Credit Union determines fair value utilizing vendors who apply matrix pricing for similar bonds where no price is observable or may compile prices from various sources. These models are primarily industry-standard models that consider various assumptions, including time value, yield curve, volatility factors, prepayment speeds, default rates, loss severity, current market and contractual prices for the underlying financial instruments, as well as other relevant economic measures. Substantially all of these assumptions are observable in the marketplace, can be derived from observable data or are supported by observable levels at which transactions are executed in the marketplace. Fair values from these models are verified, where possible, against quoted market prices for recent trading activity of assets with similar characteristics to the security being valued. Such methods are generally classified as Level 2. However, when prices from independent sources vary, cannot be obtained or cannot be corroborated, a security is generally classified as Level 3.

*Mortgage Servicing Rights*

Fair value is based on market prices for comparable servicing contracts, when available, or alternatively, is based 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. These variables change from quarter to quarter as the market conditions and projected interest rates change and may have an adverse impact on the value of the servicing right and may result in reduction to noninterest income.

### Nonrecurring Basis

Certain assets are measured at fair value on a nonrecurring basis. These assets are not measured at fair value on an ongoing basis; however, they are subject to fair value adjustments in certain circumstances, such as evidence of impairment or a change in the amount of previously recognized impairment.

(IN THOUSANDS)

## NOTE 12 FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

**Nonrecurring Basis (Continued)**

Net impairment losses related to nonrecurring fair value measurements of certain assets for the years ended December 31, 2022 and 2021 consisted of the following:

| | Carrying Value | | | |
|---|---|---|---|---|
| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Impairment Loss |
| **December 31, 2022** | | | | |
| Impaired Loans | $ - | $ - | $ 989 | $ (363) |
| **December 31, 2021** | | | | |
| Impaired Loans | $ - | $ - | $ 190 | $ (1,037) |

The Level 3 fair values were determined by estimating the value of the underlying collateral, less selling expenses.

*Impaired Loans*

In accordance with the provisions of the loan impairment guidance, impairment was measured for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement. The fair value of impaired loans is estimated using one of several methods, including collateral value, market value of similar debt, or discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. Impaired loans where an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. Collateral values are estimated using Level 3 inputs based on customized discounting criteria.

Impairment amounts on impaired loans represent specific valuation allowance and write-downs during the period presented on impaired loans that were individually evaluated for impairment based on the estimated fair value of the collateral less estimated selling costs, excluding impaired loans fully charged-off.

(IN THOUSANDS)

## NOTE 13 REVENUE FROM CONTRACTS WITH MEMBERS

The following presents noninterest income, segregated by revenue streams in-scope and out-of-scope of Topic 606, for the year ended December 31:

| | 2022 | 2021 |
|---|---|---|
| *In Scope of ASC 606:* | | |
| Services Charges on Deposits | $ 6,878 | $ 5,603 |
| Interchange Income, Net | 9,724 | 9,636 |
| Investment Advisory Fees | 16,304 | 16,725 |
| Broker-Dealer Referral Fees | 1,305 | 1,403 |
| Title and Escrow Services | 421 | 1,889 |
| Other | 3,649 | 1,355 |
| Noninterest Income in Scope of ASC 606 | 38,281 | 36,611 |
| Noninterest Income Not Within the Scope of ASC 606 (a) | 11,093 | 19,082 |
| Total Noninterest Income | $ 49,374 | $ 55,693 |

(a) This revenue is not within the scope of ASC 606, and includes fees related to loan servicing fees, gain on sale of mortgages, and credit card fees.

## NOTE 14 NAMING RIGHTS AGREEMENT

In 2019, the Credit Union entered into an agreement with the Northern Virginia Science Center Foundation (doing business as Children's Science Center) to purchase the naming rights of a science center which is anticipated to be opened no sooner than 2024. The Credit Union will retain the naming rights for 99 years. In accordance with GAAP, the Credit Union has recorded these expenses as prepaid marketing expenses, included in Other Assets on the consolidated statements of financial condition. The Credit Union will amortize these expenses ratably over a period of time determined at the date of opening. As of December 31, 2022 and 2021, the Credit Union had prepaid marketing expenses of $7,500 and $5,000, respectively.

The remaining contractual payments under this agreement as of December 31, 2022 are as follows:

| Year Ended December 31, | Amount |
|---|---|
| 2023 | $ 2,500 |