Bourns Employees Federal Credit Union

INDEPENDENT AUDITOR'S REPORT ON AUDITED FINANCIAL STATEMENTS

December 31, 2018 and 2017

RICHARDS & ASSOCIATES
Certified Public Accountants

Serving credit unions since 1967

21520 Yorba Linda Blvd., Ste. G-516
Yorba Linda, CA 92887
Msgs: (714) 287-6713
eFax: (714) 455-7082
www. RichardsCPAs.com

BOURNS EMPLOYEES FEDERAL CREDIT UNION

FINANCIAL REPORT CONTENTS
December 31, 2018 and 2017

RICHARDS & ASSOCIATES
Certified Public Accountants

21520 Yorba Linda Blvd. #G-516
Yorba Linda, California 92887
Msgs: (714) 287-6713
eFax: (714) 455-7082

Board of Directors and Supervisory Committee
Bourns Employees Federal Credit Union
Riverside, California

INDEPENDENT AUDITOR'S REPORT

Report on Financial Statements

We have audited the accompanying financial statements of Bourns Employees Federal Credit Union, which comprise the statements of financial condition as of December 31, 2018 and 2017, and the related statements of income, members’ equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management’s Responsibility for the Financial Statements

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

Auditor’s Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

INDEPENDENT AUDITOR'S REPORT *- continued*

Auditor's Responsibility *- continued*

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Bourns Employees Federal Credit Union as of December 31, 2018 and 2017, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

RICHARDS & ASSOCIATES
Certified Public Accountants

Michael E. Richards, CPA

Yorba Linda, California
March 29, 2019

BOURNS EMPLOYEES FEDERAL CREDIT UNION

STATEMENTS OF FINANCIAL CONDITION

December 31, 2018 and 2017

	2018	2017
ASSETS		
Cash and cash equivalents (Note 2)	$ 1,525,414	$ 1,138,758
Investments (Note 3)	14,795,633	14,505,978
Loans receivable, net of allowance for loan losses (Note 4)	30,426,787	28,703,187
Property & equipment (Note 5)	498,702	536,320
Accrued interest receivable	83,294	89,343
Share insurance deposit	407,840	386,071
Mortgage servicing rights (Note 12)	1,248,272	1,030,741
Core deposit intangible	132,974	149,091
Prepaid expenses and other assets	102,909	82,826
TOTAL ASSETS	$ 49,221,825	$ 46,622,315
LIABILITIES AND EQUITY		
Liabilities:		
Members' share and savings accounts (Note 6)	$ 41,196,349	$ 38,643,011
Accounts payable and other liabilities	576,860	658,665
TOTAL LIABILITIES	41,773,209	39,301,676
Commitments and contingent liabilities (Note 8)		
Members' equity, substantially restricted		
Appropriated (regular reserve)	952,125	952,125
Unappropriated (undivided earnings)	5,998,943	5,829,706
Equity acquired through merger	549,410	549,410
	7,500,478	7,331,241
Accumulated other comprehensive income	(51,862)	(10,602)
TOTAL MEMBERS’ EQUITY	7,448,616	7,320,639
TOTAL LIABILITIES AND MEMBERS’ EQUITY	$ 49,221,825	$ 46,622,315

The accompanying notes are an integral part of these financial statements.

BOURNS EMPLOYEES FEDERAL CREDIT UNION

STATEMENTS OF INCOME

Years ended December 31, 2018 and 2017

	2018	2017
INTEREST INCOME		
Loans	$ 1,177,774	$ 1,058,452
Investments	350,203	270,195
TOTAL INTEREST INCOME	1,527,977	1,328,647
INTEREST EXPENSE		
Members' share and savings accounts	265,985	204,516
Borrowed funds	67	164
TOTAL INTEREST EXPENSE	266,052	204,680
NET INTEREST INCOME	1,261,925	1,123,967
PROVISION FOR LOAN LOSSES (CREDIT)	6,394	(42,799)
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	1,255,531	1,166,766
NON-INTEREST INCOME		
Service charges and other income	311,539	368,733
Rental income	-	9,925
Gain on servicing assets	490,371	702,242
Gain on bargain purchase	-	38,294
TOTAL NON-INTEREST INCOME	801,910	1,119,194
NON-INTEREST EXPENSE		
General and administrative expenses		
Compensation and benefits	968,816	970,818
Office operations	384,853	351,580
Other expenses	398,862	399,954
Other non-operating activities	35,656	68,575
Loss on investments write-down	100,000	-
Loss on sale or disposal of property and equipment	17	109
TOTAL NON-INTEREST EXPENSES	1,888,204	1,791,036
NET INCOME	$ 169,237	$ 494,924

The accompanying notes are an integral part of these financial statements.

STATEMENTS OF COMPREHENSIVE INCOME

Years ended December 31, 2018 and 2017

		2018		2017
NET INCOME	$	169,237	$	494,924
Net change in unrealized (loss) gain on available-for-sale securities		(41,260)		30,794
TOTAL COMPREHENSIVE INCOME	$	127,977	$	525,718

The accompanying notes are an integral part of these financial statements.

BOURNS EMPLOYEES FEDERAL CREDIT UNION

STATEMENTS OF MEMBERS' EQUITY
Years ended December 31, 2018 and 2017

	2018	2017
APPROPRIATED - REGULAR RESERVE		
Beginning / Ending balance	$ 952,125	$ 952,125
UNAPPROPRIATED - UNDIVIDED EARNINGS		
Beginning balance	5,829,706	5,334,782
Net income	169,237	494,924
Ending balance	5,998,943	5,829,706
EQUITY ACQUIRED THROUGH MERGER		
Beginning / Ending balance	549,410	549,410
ACCUMULATED OTHER COMPREHENSIVE LOSS		
Beginning balance	(10,602)	(41,396)
Net change in unrealized (loss) gain on available-for-sale securities	(41,260)	30,794
Ending balance	(51,862)	(10,602)
TOTAL MEMBERS' EQUITY	$ 7,448,616	$ 7,320,639

The accompanying notes are an integral part of these financial statements.

STATEMENTS OF CASH FLOWS
Years ended December 31, 2018 and 2017

	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 169,237	$ 494,924
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses (credit)	6,394	(42,799)
Depreciation and amortization	45,094	37,777
Premium amortization net of discount accretion	809	(513)
Stock dividends added to investments	(6,042)	(5,667)
Capitalization of mortgage servicing rights	(490,371)	(702,242)
Amortization of mortgage servicing rights	272,840	210,378
Amortization of premium on loans	11,574	8,681
Amortization of core deposit intangible	16,117	12,089
Gain on merger	-	(38,294)
Loss on investments write-down	100,000	-
Loss on property and equipment	-	109
Changes in operating assets and liabilities:		
Decrease (increase) in accrued interest receivable	6,049	(8,054)
(Increase) decrease in prepaid expenses and other assets	(20,083)	9,179
(Decrease) increase in accounts payable and other liabilities	(81,805)	92,857
Total adjustments	(139,424)	(426,499)
Net cash provided by operating activities	29,813	68,425
CASH FLOWS FROM INVESTING ACTIVITIES:		
Cash acquired from merger with Bakery Employees Credit Union	-	1,965,957
Loans granted, net of principal collection	(1,741,568)	(2,574,708)
Sale or maturing of securities	287,818	363,617
Net increase in capital stock at Federal Home Loan Bank of San Francisco	(500)	(18,900)
Decrease in deposits in financial institutions	(713,000)	(463,000)
Increase in share insurance deposit	(21,769)	(21,251)
Purchase of property and equipment, net of disposals	(7,476)	(83,505)
Net cash used in investing activities	(2,196,495)	(831,790)

The accompanying notes are an integral part of these financial statements.

BOURNS EMPLOYEES FEDERAL CREDIT UNION

STATEMENTS OF CASH FLOWS - *continued*

Years ended December 31, 2018 and 2017

	2018	2017
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in members' share and savings accounts	$ 2,553,338	$ 1,203,635
Net cash provided by financing activities	2,553,338	1,203,635
NET INCREASE IN CASH AND CASH EQUIVALENTS	386,656	440,270
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	1,138,758	698,488
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 1,525,414	$ 1,138,758

SUPPLEMENTAL DISCLOSURES:

	2018	2017
Cash received during the year from interest on loans and investments	$ 1,540,367	$ 1,323,094
Cash paid during the year for dividends	$ 265,985	$ 204,516

The accompanying notes are an integral part of these financial statements.

NOTE 1: ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Organization: Bourns Employees Federal Credit Union (Credit Union) is organized under the Federal Credit Union Act. Participation in the Credit Union is limited to those individuals who qualify for membership. The field of membership is defined in the Credit Union's bylaws.

Nature of business: The Credit Union provides a variety of financial services to its members, many of whom are employees or former employees of Bourns, Inc., individuals who live or work in the Riverside County area, selected employee groups, and their qualifying family members. The Credit Union’s primary source of revenue is interest from loans and investments.

Use of estimates: The preparation of financial statements, in conformity with generally accepted accounting principles in the United States of America (GAAP), 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 financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. A material estimate that is particularly susceptible to significant change in the near term relates to the determination of the allowance for loan losses and fair value of financial instruments.

Cash and cash equivalents: For the purpose of the statements of financial condition and the statements of cash flows, cash and cash equivalents include cash on hand, amounts due from financial institutions, and investments with original maturity of three months or less. Amounts due from financial institutions may, at times, exceed federally insured limits.

Investments: Certificates of deposit are generally non-negotiable and non-transferable, and may incur substantial penalties for withdrawal prior to maturity. Certificates of deposit investments are stated at cost and are federally insured up to a maximum of $250,000 by the National Credit Union Administration (NCUA) or Federal Deposit Insurance Corporation (FDIC). Included with investments is a member capital account in a corporate credit union.

Negotiable securities are classified in accordance with the Credit Union's asset/liability management and investment policies. The following is a description of the classification and accounting procedures used for investments:

NOTE 1: ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES – *continued*

Investments – continued:

> Available-for sale: Investments that are not purchased principally to be sold in the near term nor with the positive intent and ability to hold until maturity as well as those without a defined maturity and could be sold in response to rate changes, prepayment risk, liquidity, availability of and the yield on alternative investments and other market and economic factors are classified as available-for-sale. These securities are marked to market, with unrealized gains or losses not affecting earnings but shown as a separate component of the equity portion of the balance sheet. Unrealized gains and losses on available-for-sale securities are recognized as direct increases or decreases in other comprehensive income.

Purchase premiums and discounts are recognized in interest income over the term of the securities. Declines in the fair value of available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment (OTTI) losses, Management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Credit Union to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. Gains and losses on the sale of securities are recorded on the trade date and the costs of securities sold are determined using the specific identification method.

The Credit Union does not maintain a trading portfolio. Other investments are classified separately, stated at cost and subject to OTTI evaluation.

Loans to members: The Credit Union originates mortgage loans both for sale and for its own portfolio. The Credit Union originated approximately $34,700,000 and $49,850,000 of first mortgage loans for its members in the years ended December 31, 2018 and 2017, respectively. Approximately $32,360,000 and $46,520,000 of mortgages were sold in the years ended December 31, 2018 and 2017, respectively.

Loans receivable: Loans receivable are stated at unpaid principal balance, net of any unamortized premiums or discounts less an allowance for loan losses. Interest on loans is recognized over the term of the loan and is calculated using the simple-interest method for consumer loans and home equity loans and the day count convention method for first mortgage real estate loans on principal amounts outstanding. When principal or interest is delinquent for sixty days or more, the Credit Union evaluates the loan for nonaccrual status.

NOTE 1: ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES – *continued*

Loans receivable - continued: After a loan is placed on nonaccrual status, all interest previously accrued but not collected is reversed against current period interest income. Subsequent collections of interest payments on nonaccrual loans are recognized as interest income unless ultimate collectability of the loan is in doubt. Cash collections on loans where ultimate collectability remains in doubt are applied as reductions of the loan principal balance and no interest income is recognized until the principal balance has been collected.

Loan fees and certain direct loan origination costs are deferred, and the net cost is recognized as an adjustment to interest income using the interest method over the contractual life of the loans, adjusted for estimated prepayments based on the Credit Union's historical prepayment experience.

Allowance for loan losses: The allowance for loan losses reflects Management's judgment of probable loan losses inherent in the portfolio at the balance sheet date. The Credit Union uses a disciplined process and methodology to establish the allowance for loan losses each quarter. To determine the total allowance for loan losses, Management estimates the reserves needed for each segment of the portfolio, including loans analyzed individually and loans analyzed on a pooled basis. The allowance for loan losses consists of amounts applicable to: (i) the auto secured loans portfolio; (ii) the real estate loans portfolio; (iii) the consumer loans portfolio and (iv) the unsecured and credit card loans portfolio.

To determine the balance of the allowance account, loans are pooled by portfolio segment and losses are modeled using historical experience and quantitative and other mathematical techniques over the loss emergence period. Management exercises significant judgment in determining the estimation method that fits the credit risk characteristics of each portfolio segment. Management must use judgment in establishing additional input metrics for the modeling processes. The models and assumptions used to determine the allowance are independently validated and reviewed to ensure that their theoretical foundation, assumptions, data integrity, computational processes, reporting practices, and end-user controls are appropriate and properly documented.

The establishment of the allowance for loan losses relies on a consistent process that requires multiple layers of Management review and judgment and responds to changes in economic conditions, member behavior, and collateral value, among other influences. From time to time, events or economic factors may affect the loan portfolio, causing Management to provide additional amounts to or release balances from the allowance for loan losses. The Credit Union's allowance for loan losses is sensitive to risk ratings assigned to individually evaluated loans and economic assumptions and delinquency trends driving statistically modeled reserves. Individual loan risk ratings are evaluated based on each situation by experienced senior credit officers.

NOTE 1: ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES – *continued*

Allowance for loan losses – continued: Management monitors differences between estimated and actual incurred loan losses. This monitoring process includes periodic assessments by Senior Management of the loan portfolios and the models used to estimate incurred losses in those portfolios. Additions to the allowance for loan losses are made by charges to provision for loan losses. Credit exposures deemed to be uncollectible are charged against the allowance for loan losses. Recoveries of previously charged off amounts are credited to the allowance for loan losses.

Loan charge-offs: For consumer loans, the Credit Union generally fully or partially charges down to the fair value of collateral securing the asset when:

- Management judges the asset to be uncollectible;
- repayment is deemed to be protracted beyond reasonable time frames;
- the asset has been classified as a loss by either the Credit Union's internal loan review process or external examiners;
- the member has filed bankruptcy and the loss becomes evident owing to a lack of assets; or
- the loan is one hundred eighty days past due unless both well secured and in the process of collection.

The Credit Union's charge-off policies by segment of the loan portfolio are as follows:

- *Real estate loans* – The Credit Union generally writes down to the net realizable value when the loan is one hundred eighty days past due.
- *Auto loans* – The Credit Union generally fully or partially charges down to the net realizable value when the loan is one hundred eighty days past due.
- *Unsecured loans* – The Credit Union generally charges off when the loan is one hundred eighty days past due.
- *Credit cards loans* – The Credit Union generally fully charges off when the loan is one hundred eighty days past due.
- *Other secured loans* – The Credit Union generally fully or partially charges down to the net realizable value when the loan is one hundred eighty days past due.

NOTE 1: ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES – *continued*

Troubled debt restructurings: In situations where, for economic or legal reasons related to a member's financial difficulties, the Credit Union grants a concession for other than an insignificant period of time to the member that the Credit Union would not otherwise consider, if applicable, the related loan is classified as a troubled debt restructuring (TDR). The Credit Union strives to identify members in financial difficulty early and works with them to modify to more affordable terms before their loan reaches nonaccrual status. These modified terms may include rate reductions, principal forgiveness, payment forbearance and other actions intended to minimize the economic loss and to avoid foreclosure or repossession of the collateral. In cases where the Credit Union grants the member new terms that provide for a reduction of either interest or principal, the Credit Union measures any impairment on the restructuring as previously noted for impaired loans.

In addition to the allowance for the pooled portfolios, the Credit Union develops a separate allowance for loans that are identified as impaired through a TDR. As soon as the Credit Union determines that a loan under TDR is current and performing under the restructured payment, and after review, the Credit Union believes the status will continue, the loan is moved back into the respective segment or class and the allowance is calculated using the pooling method for the respective pool.

Property and equipment: Land is carried at cost. Other fixed assets are carried at cost, less accumulated depreciation and amortization. Fixed assets are depreciated using the straight-line method over the estimated useful lives of the assets.

Transfers of financial assets: The Credit Union accounts for transfers and servicing of financial assets in accordance with FASB ASC 860, *Transfers and Servicing*. 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 obtains 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.

Servicing: Mortgage servicing assets are recognized separately when 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 subsequently measures each class of servicing asset using either the fair value or the amortization method. The Credit Union has elected to initially and subsequently measure the mortgage servicing rights for consumer mortgage loans using the amortization method.

NOTE 1: ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES – *continued*

Servicing – continued: Under the amortization method, servicing rights are amortized in proportion to and over the period of estimated net servicing income. The amortized assets are assessed for impairment or increased obligation based on the fair value at each reporting date.

Fair value is based on market prices for comparable mortgage 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 market conditions and projected interest rates change, and may have an adverse impact on the value of the mortgage servicing right and may result in a reduction to noninterest income.

Valuation of long-lived assets: Long-lived assets and certain identifiable intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Management reviews all material assets annually for possible impairment. If such assets are considered to be impaired, the impairment recognized is measured as the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets.

Share insurance deposit: Each member's share and savings account is insured up to $250,000 by the National Credit Union Share Insurance Fund (NCUSIF). The deposit in the NCUSIF is in accordance with regulations set forth by the National Credit Union Administration (NCUA), which require the maintenance of a deposit by each insured credit union in an amount equal to one percent of its insured shares. The deposit would be refunded to the Credit Union if its insurance coverage is terminated, it converts to insurance coverage from another source, or the operations of the fund are transferred from the NCUA Board. The Credit Union is required to pay annual assessments as determined by the NCUA Board.

Individual deposits in excess of the NCUSIF insured limit are insured by a private insurance company, American Share Insurance Corporation (ASI), subject to their policy limit of $250,000. There is no limitation as to the number of accounts a member can have under ASI's coverage. ASI requires the maintenance of a deposit by each insured credit union in an amount equal to 1% of the Credit Union’s maximum limit liability of $1,500,000. The Credit Union maintains a deposit with ASI in the amount of $30,000.

In February 2018, the National Credit Union Administration (NCUA) Board unanimously approved share insurance distribution of $736 million to eligible federally insured credit unions in the third quarter of 2018. The Credit Union received $29,051 in July 2018.

NOTE 1: ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES – *continued*

NCUSIF insurance premiums: A credit union is required to pay an annual insurance premium based on a percent of its total insured shares, unless the payment is waived or reduced by the NCUA Board.

Members' share and savings accounts: Members' shares are the savings deposit accounts of the owners of the Credit Union. Share ownership entitles the members to vote in the annual elections of the Board of Directors and on other corporate matters. Irrespective of the amount of shares owned, no member has more than one vote. Members' shares are subordinated to all other liabilities of the Credit Union in the event of liquidation. Interest on share and savings accounts is based on available earnings at the end of an interest period and is not guaranteed by the Credit Union. Interest rates on share and savings accounts are set by the Board of Directors, based on an evaluation of current and future market conditions.

Members' equity: The Credit Union is required by regulation to maintain a statutory reserve. This reserve, which represents a regulatory restriction of retained earnings, is not available for the payment of interest.

Income taxes: The Credit Union is exempt, by statute, from federal and state income taxes under the provisions of the Internal Revenue Code.

Off-balance-sheet 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.

Comprehensive income (loss): Comprehensive income (loss) consists of net income (loss) and other comprehensive income (loss) that includes unrealized gains and losses on securities available-for-sale.

Retirement plans: The Credit Union has a contributory 401(k) retirement plan for all employees who have met both tenure and minimum age requirements specified in the plan through Bourns, Inc.

Presentation of comparative financial statements: To more clearly illustrate the financial condition of the Credit Union and the results of its operations, the current year financial information is presented along with the previous year. Financial information presented for the previous year may be classified differently than originally disclosed. These reclassifications, which do not affect the auditor's report on those financial statements, were made for purposes of comparison.

NOTES TO FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 2: CASH AND CASH EQUIVALENTS

Cash and cash equivalents, including investments with original maturity of three months or less, are as follows:

	December 31,	
	2018	2017
Cash on hand	$ 148,160	142,287
Cash on deposit	1,377,254	996,471
	$ 1,525,414	$ 1,138,758

NOTE 3: INVESTMENTS

The carrying and estimated fair values of investments are as follows:

	December 31,	
	2018	2017
CERTIFICATES OF DEPOSIT	$ 12,688,000	$ 11,975,000

	December 31,	
	2018	2017
CONTRIBUTED CAPITAL ACCOUNT	$ 92,410	$ 92,410

The member contributed capital account is invested in Catalyst Corporate Federal Credit Union. This deposit is a permanent capital contribution. This investment is not publicly traded; therefore, it is not practical to determine its fair value. The amortized cost approximates the fair value.

NOTE 3: INVESTMENTS – *continued*

NEGOTIABLE SECURITIES

	December 31, 2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
Mortgage-backed securities guaranteed by U.S. government sponsored enterprises	$ 1,799,801	$ 33,590	$ 85,452	$ 1,747,939
Capital stock, Federal Home Loan Bank	178,200	-	-	178,200
Capital stock, credit union service organizations	89,084	-	-	89,084
	$ 2,067,085	$ 33,590	$ 85,452	$ 2,015,223

Included with mortgage backed securities guaranteed by U.S. Government sponsored enterprises above are collateralized mortgage obligations with amortized cost of $126,765 and fair market value of $147,073 as of December 31, 2018.

NOTE 3: INVESTMENTS – *continued*

NEGOTIABLE SECURITIES – *continued*

	December 31, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
Mortgage-backed securities guaranteed by U.S. government sponsored enterprises	$ 2,088,428	$ 39,212	$ 49,814	$ 2,077,826
Capital stock, Federal Home Loan Bank	177,700	-	-	177,700
Capital stock, credit union service organizations	183,042	-	-	183,042
	$ 2,449,170	$ 39,212	$ 49,814	$ 2,438,568

Included with mortgage backed securities guaranteed by U.S. Government sponsored enterprises above are collateralized mortgage obligations with amortized cost of $155,157 and fair market value of $178,617 as of December 31, 2017.

Investments in Credit Union Service Organizations and Federal Home Loan Bank of San Francisco are not publicly traded; therefore, it is not practical to determine these fair values. The amortized cost approximates the fair value.

The credit union had $120,000 invested in Member Business Lending LLC as of December 31, 2017. The investment was written down to $20,000 as of December 31, 2018.

NOTE 3: INVESTMENTS – *continued*

NEGOTIABLE SECURITIES – *continued*

Information pertaining to securities with gross unrealized losses as of December 31, 2018 and 2017, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, follows:

	December 31, 2018			
		Continuous Unrealized Losses Existing for		
	Fair Value	Less than 12 months	More than 12 months	Total Unrealized Losses
Available-for-sale:				
Mortgage-backed securities guaranteed by U.S. government sponsored enterprises	$ 1,537,348	-	$ 85,452	$ 85,452
	$ 1,537,348	-	$ 85,452	$ 85,452

	December 31, 2017			
		Continuous Unrealized Losses Existing for		
	Fair Value	Less than 12 months	More than 12 months	Total Unrealized Losses
Available-for-sale:				
Mortgage-backed securities guaranteed by U.S. government sponsored enterprises	$ 1,812,105	$ 2,747	$ 47,067	$ 49,814
	$ 1,812,105	$ 2,747	$ 47,067	$ 49,814

NOTE 3: INVESTMENTS – *continued*

NEGOTIABLE SECURITIES – *continued*

The accounting standards provide a framework for measuring fair value and further defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The Credit Union determines the fair values of its financial instruments based on the fair value hierarchy established in generally accepted accounting principles (GAAP), which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

This framework describes three levels of inputs that may be used to measure fair value. Financial instruments are considered level 1 when valuation can be based on quoted prices in active markets for identical assets or liabilities. Financial instruments are considered level 2 when they are generally valued using quoted prices for similar assets. The fair value of available-for-sale securities is based on quoted market prices or market prices for similar assets. Financial instruments are considered level 3 when valuation is calculated by the use of pricing models and/or discounted cash flow methodologies or valuation requires significant management judgment or estimation. The Credit Union does not use level 3 pricing.

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given, among other things, to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Credit Union to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

Market changes in interest rates and market changes in credit spreads will cause normal fluctuations in the market price of securities and the possibility of temporary unrealized losses. The reason for the temporary loss is that market interest rates are higher than when these securities were originally purchased. The Credit Union reviews all of its securities for impairment periodically. The Credit Union has determined that there was no other-than-temporary impairment associated with these securities as of December 31, 2018.

NOTE 3: INVESTMENTS - *continued*

NEGOTIABLE SECURITIES – *continued*

A summary of investments by contractual maturity is shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	December 31,	
	2018	2017
Within one year	$ 5,121,000	$ 4,119,000
One to five years	7,471,000	7,760,000
Over five years	96,000	96,000
Investments with monthly principal payments	1,799,801	2,088,428
Subtotal	14,487,801	14,063,428
Investments without a defined maturity	359,694	453,152
	$ 14,847,495	$ 14,516,580

Accrued interest receivable on investments amounted to $23,622 and $29,977 as of December 31, 2018 and 2017, respectively.

NOTE 4: LOANS RECEIVABLE

The composition of loans receivable is as follows:

	December 31,	
	2018	2017
Real estate	$ 18,281,754	$ 17,965,907
Automobile	5,605,003	4,707,521
Credit cards	3,014,185	2,536,189
Home equity lines of credit	2,298,429	1,530,267
Other loans	1,194,224	1,295,696
Commercial loans	368,276	1,040,482
	30,761,871	29,076,062
Discount on loans, net of premium	(35,186)	(16,297)
Allowance for loan losses	(299,898)	(356,578)
	$ 30,426,787	$ 28,703,187

Accrued interest receivable on loans amounted to $59,672 and $59,366 as of December 31, 2018 and 2017, respectively.

NOTE 4: LOANS RECEIVABLE - *continued*

The acquisition of Bakery Employees Credit Union in February 2017 resulted in a net discount of $14,931 which includes both an adjustment to the fair value of the loan portfolio and the estimated credit risk in the portfolio. There was a net loan recovery of $7,315 for the year ending December 31, 2018 and a net loan charged off of $7,315 for the year ending December 31, 2017. The Credit Union amortized $11,574 and $8,681 from the loss on acquired loans for the years ending December 31, 2018 and 2017, respectively. The net discount amounted to $35,186 and $16,297 as of December 31, 2018 and 2017, respectively.

Allowance for loan losses: The Credit Union has an established methodology to determine the adequacy of the allowance for loan losses that assesses the risks and losses inherent in the Credit Union's portfolio. For purposes of determining the allowance for loan losses, the Credit Union segments certain loans in its portfolio by product type. The Credit Union's loans are segmented into the following pools: auto loan portfolio, real estate loan portfolio, consumer secured loan portfolio, and consumer unsecured loan portfolio. The Credit Union also sub-segments three of these segments into classes based on the associated risks within those segments. Real estate loans are divided into the following six classes: (a) first mortgage loans with fixed interest rate, (b) first mortgage loans with variable interest rate, (c) first mortgage for investment property loans, (d) second mortgage loans, (e) home equity lines of credit loans, and (f) mortgage loans under modification. Consumer secured loans are divided into the following two classes: (a) share secured loans and (b) miscellaneous secured loans. Consumer unsecured loans are divided into the following five classes: (a) classic credit card loans, (b) gold credit card loans, (c) platinum credit card loans, (d) signature loans, and (e) consumer loans under modification. Each class of loans requires significant judgment to determine the estimation method that fits the credit risk characteristic of its portfolio segment. Management must use judgment in establishing additional input metrics for the modeling processes. The models and assumptions that the Credit Union uses to determine the allowance are independently validated and reviewed to ensure that their theoretical foundation, assumptions, data integrity, computational processes, reporting practices, and end-user controls are appropriate and properly documented.

The following are the factors that the Credit Union uses to determine the balance of the allowance account for each segment or class of loans.

Auto loans: Auto loans include loans secured by new auto or used auto. These loans are not assessed at an underlying class level. A historical loss percentage is applied to the segment. The historical loss percentage is calculated using a twelve months, twenty-four months, and thirty-six months ratio and the period with the highest historical loss percentage is used. The historical loss period as of December 31, 2018 was twelve months.

Based on the Credit Union's assessment on credit risk and analysis of leading predictors of losses, the Credit Union may apply additional loss multipliers to loan balances. As of December 31, 2018, the Credit Union considered additional loss estimations based on the loan delinquency category, bankruptcy category, and collateral value.

NOTE 4: LOANS RECEIVABLE - *continued*

Allowance for loan losses - continued:

Real estate loans: Real estate loans are pooled by portfolio class and a historical loss percentage is applied to each class. Historical loss percentage time frames may vary between classes. These time frames are based on historical loss experience modeling and other quantitative and mathematical migration techniques over the loss emergence period. The historical loss percentage is calculated using a twelve months, twenty-four months, and thirty-six months ratio and the period with the highest historical loss percentage is used. The historical loss period as of December 31, 2018 was thirty-six months.

The Credit Union estimates an additional component of the allowance for loan losses for the non-impaired real estate segment through the application of loss factors to loans grouped by their individual credit risk rating categories. These ratings reflect the estimated default probability and quality of underlying collateral. The loss factors used are statistically derived through the observation of losses incurred for loans within each internal credit risk rating over a specified period of time.

In addition, based on the Credit Union's analysis of leading predictors of losses, the Credit Union may apply additional loss multipliers to the loan balances. Currently, the Credit Union may consider additional loss estimations based on the average foreclosure rate where the properties are located, the loan delinquency category, bankruptcy category, and collateral value.

Consumer secured portfolio: Consumer secured loans include loans secured by shares or other collateral. Consumer secured loans are pooled by portfolio class and a historical loss percentage is applied to each class. The historical loss percentage is calculated using a twelve months, twenty-four months, and thirty-six months ratio and the period with the highest historical loss percentage is used. As of December 31, 2018, the historical loss time frame for each class was twelve months.

Based on the Credit Union's assessment on credit risk and analysis of leading predictors of losses, the Credit Union may apply additional loss multipliers to loan balances. As of December 31, 2018, the Credit Union considered additional loss estimations based on the loan delinquency category, bankruptcy category, and collateral value.

NOTE 4: LOANS RECEIVABLE - *continued*

Allowance for loan losses - continued:

Consumer unsecured portfolio: Unsecured consumer loans are pooled by portfolio class and a historical loss percentage is applied to each class. Historical loss percentage time frames may vary between classes. These time frames are based on historical loss experience modeling and other quantitative and mathematical migration techniques over the loss emergence period. The historical loss percentage is calculated using a twelve months, twenty-four months, and thirty-six months ratio and the period with the highest historical loss percentage is used. As of December 31, 2018, the historical loss time frame for each class was as follows:

Classic credit card loans – twenty-four months
Gold credit card loans – twelve months
Platinum credit card loans – thirty-six months
Signature loans – twenty-four months
Consumer loans under modification – thirty-six months

Based on the Credit Union's assessment on credit risk and analysis of leading predictors of losses, the Credit Union may apply additional loss multipliers to loan balances. As of December 31, 2018, the Credit Union considered additional loss estimations based on the loan delinquency category and bankruptcy category.

The Credit Union's estimation process: The Credit Union estimates loan losses under multiple economic scenarios to establish a range of potential outcomes for each criterion the Credit Union applies to the allowance calculation. Management applies judgment to develop its own view of loss probability within that range, using external and internal parameters with the objective of establishing an allowance for the losses inherent within these portfolios as of the reporting date.

Loans by Segment: The total allowance reflects Management's estimate of loan losses inherent in the loan portfolio as of December 31, 2018 and 2017. The Credit Union considers the allowance for loan losses of $299,898 and $356,578 adequate to cover loan losses inherent in the loan portfolio as of December 31, 2018 and 2017, respectively. The following tables present by portfolio segment, the changes in the allowance for loan losses and the loans receivable.

NOTE 4: LOANS RECEIVABLE - *continued*

Allowance for loan losses - continued:

Loans by Segment - *continued*:

Allowance for Loan Losses and Receivable in Loans
For the Year Ended December 31, 2018

	Real Estate	Consumer	Credit Cards	Total
Allowance for Loan Losses:				
Beginning balance	$ 176,054	$ 111,250	$ 69,274	$ 356,578
Charge-offs	-	(48,040)	(29,909)	(77,949)
Recoveries	-	3,368	11,507	14,875
Provision for loan losses (credit)	(15,707)	(6,685)	28,786	6,394
Ending balance	$ 160,347	$ 59,893	$ 79,658	$ 299,898
Ending balance:				
• individually evaluated for impairment	160,347	14,350	19,849	194,546
• collectively evaluated for impairment	-	45,543	59,809	105,352
	$ 160,347	$ 59,893	$ 79,658	$ 299,898
Loans Receivable:				
Ending balance:				
• individually evaluated for impairment	1,699,059	43,255	36,879	1,779,193
• collectively evaluated for impairment	19,249,400	6,755,972	2,977,306	28,982,678
	$ 20,948,459	$ 6,799,227	$ 3,014,185	$ 30,761,871

NOTE 4: LOANS RECEIVABLE - *continued*

Allowance for loan losses - continued:

Loans by Segment - *continued*:

Allowance for Loan Losses and Receivable in Loans
For the Year Ended December 31, 2017

	Real Estate	Consumer	Credit Cards	Total
Allowance for Loan Losses:				
Beginning balance	$ 312,798	$ 33,878	$ 111,217	$ 457,893
Charge-offs	-	(20,382)	(60,022)	(80,404)
Recoveries	-	9,800	12,088	21,888
Provision for loan losses (credit)	(136,744)	87,954	5,991	(42,799)
Ending balance	$ 176,054	$ 111,250	$ 69,274	$ 356,578
Ending balance:				
• individually evaluated for impairment	176,054	83,427	20,934	280,415
• collectively evaluated for impairment	-	27,823	48,340	76,163
	$ 176,054	$ 111,250	$ 69,274	$ 356,578
Loans Receivable:				
Ending balance:				
• individually evaluated for impairment	2,095,286	107,900	20,934	2,224,120
• collectively evaluated for impairment	18,441,370	5,895,317	2,515,255	26,851,942
	$ 20,536,656	$ 6,003,217	$ 2,536,189	$ 29,076,062

Changes in accounting methodology: For the year ended December 31, 2018, there were no significant changes in the accounting methodology for the allowance for loan losses.

NOTE 4: LOANS RECEIVABLE - *continued*

Credit quality information: Payment activity is reviewed by Management periodically to determine how loans are performing. Loans are considered to be nonperforming when days delinquent is greater than sixty days.

Nonperforming loans would also include certain loans that have been modified in TDRs where economic concessions have been granted to borrowers who have experienced or are expected to experience financial difficulties. These concessions typically result from the Credit Union's loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance or other actions. Certain TDRs would be classified as nonperforming at the time of restructure and may only be returned to performing status after considering the borrower's sustained repayment performance for a reasonable period. There were no non-performing real estate loans as of December 31, 2018.

Age analysis of past due loans receivable by class: Following are tables which include an aging analysis of past due loans receivable as of December 31, 2018 and 2017. Also included are loans that are sixty days or more past due as to interest and principal and still accruing, because they are (a) well-secured and in the process of collection or (b) real estate loans or (c) loans exempt under regulatory rules from being classified as nonaccrual.

Credit Quality Information
Age Analysis of Past Due Loans Receivable by Class
As of December 31, 2018

	30-59 Days Past Due	60 Days Past Due or Greater	Total Past Due	Current	Total Loans Receivable
Real estate	$ 146,392	$ -	$ 146,392	$ 20,802,067	$ 20,948,459
Consumer	52,262	43,255	95,517	6,703,710	6,799,227
Credit cards	51,546	36,879	88,425	2,925,760	3,014,185
Total	$ 250,200	$ 80,134	$ 330,334	$ 30,431,537	$ 30,761,871

NOTES TO FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 4: LOANS RECEIVABLE - *continued*

Age analysis of past due loans receivable by class - continued:

Credit Quality Information
Age Analysis of Past Due Loans Receivable by Class
As of December 31, 2017

	30-59 Days Past Due	60 Days Past Due or Greater	Total Past Due	Current	Total Loans Receivable
Real estate	$ -	$ -	$ -	$ 20,536,656	$ 20,536,656
Consumer	124,436	48,253	172,689	5,830,528	6,003,217
Credit cards	7,071	20,934	28,005	2,508,184	2,536,189
Total	$ 131,507	$ 69,187	$ 200,694	$ 28,875,368	$ 29,076,062

Impaired loans: The Credit Union considers a loan to be impaired when, based on current information and events, the Credit Union determines that it will not be able to collect all amounts due according to the loan contract, including scheduled interest payments. Determination of impairment is treated the same across all classes of loans. When the Credit Union identifies a loan as impaired, the Credit Union measures the impairment based on the present value of expected future cash flows, discounted at the loan's effective interest rate, except when the sole (remaining) source of repayment for the loan is the operation or liquidation of the collateral. In these cases, the Credit Union uses the current fair value of the collateral, less selling costs when foreclosure is probable, instead of discounted cash flows. If the Credit Union determines that the value of the impaired loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs and unamortized premium or discount), the Credit Union recognizes impairment through an allowance estimate or a charge-off to the allowance. The Credit Union determines impairment based on a sixty-day default period and all loans classified as TDRs.

When the ultimate collectability of the total principal of an impaired loan is in doubt and the loan is on nonaccrual status, all payments are applied to principal, under the cost recovery method. When the ultimate collectability of the total principal of an impaired loan is not in doubt and the loan is on nonaccrual status, contractual interest is credited to interest income when received, under the cash basis method.

Nonaccrual loans: The Credit Union generally places loans on nonaccrual status when the full and timely collection of interest or principal becomes uncertain, part of the principal balance has been charged off and no restructuring has occurred, or the loans reach sixty days past due.

NOTE 4: LOANS RECEIVABLE - *continued*

Nonaccrual loans - continued: When the Credit Union places a loan on nonaccrual status, the Credit Union reverses the accrued unpaid interest receivable against interest income and accounts for the loan on the cash or cost recovery method, until it qualifies for return to accrual status. Generally, the Credit Union returns a loan to accrual status when (a) all delinquent interest and principal become current under the terms of the loan agreement or (b) the loan is both well-secured and in the process of collection and collectability is no longer doubtful.

The Credit Union has determined that the entire balance of a loan is contractually delinquent for all classes if the minimum payment is not received by the specified due date on the member's statement. Interest and fees continue to accrue on past due loans until the date the loan goes into nonaccrual status, if applicable. As of December 31, 2018, $31,797 of loans were placed on nonaccrual status with approximately $600 of accrued interest not recognized in the financial statements.

NOTE 5: PROPERTY AND EQUIPMENT

Property and equipment are summarized as follows:

	December 31,	
	2018	2017
Land	$ 250,000	$ 250,000
Building and improvements	190,059	190,059
Furniture, fixtures, and equipment	225,186	224,360
Subtotal	665,245	664,419
Accumulated depreciation and amortization	(166,543)	(128,099)
	$ 498,702	$ 536,320

Depreciation and amortization expense amounted to $45,094 and $37,777 for the years ended December 31, 2018 and 2017, respectively.

NOTE 6: MEMBERS' SHARE AND SAVINGS ACCOUNTS

Shares and savings accounts are summarized as follows:

	December 31,	
	2018	2017
Share drafts	$ 2,729,354	$ 2,590,726
Share savings	20,265,318	20,398,982
Other deposits	18,201,677	15,653,303
	$ 41,196,349	$ 38,643,011

The aggregate amounts of uninsured members' share and savings accounts were approximately $1,610,000 and $860,000 as of December 31, 2018 and 2017, respectively.

A summary by maturity of members' share and savings accounts is as follows:

	December 31,	
	2018	2017
No contractual maturity	$ 25,574,791	$ 25,996,374
Within one year	9,314,762	8,715,733
One to three years	4,896,951	3,231,182
Over three years	1,409,845	699,722
	$ 41,196,349	$ 38,643,011

Interest rates are set by the Board of Directors, based on an evaluation of current and future market conditions.

NOTE 7: BORROWED FUNDS

The Credit Union maintains two line of credit agreements with Catalyst Corporate Federal Credit Union at a rate to be determined by the lender when funds are borrowed. As of December 31, 2018 and 2017, the Credit Union had no outstanding balances on the lines of credit but could borrow up to $2,500,000.

NOTE 8: COMMITMENTS AND CONTINGENT LIABILITIES

The Credit Union is a party to various legal actions normally associated with financial institutions, the aggregate effect of which, in Management's and legal counsel's opinion, would not be material to the Credit Union's financial condition.

NOTE 8: COMMITMENTS AND CONTINGENT LIABILITIES - *continued*

The principal commitments of the Credit Union are as follows:

Financial instruments with off-balance sheet risk: The Credit Union is a 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 the amount recognized in the financial statements.

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

These financial instruments include commitments for lines of credit, credit cards, and home equity lines of credit. The contract amounts represent credit risk totaling approximately $9,100,000 and $9,220,000 as of December 31, 2018 and 2017, respectively.

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. Since 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, if deemed necessary by the Credit Union upon extension of credit, is based on Management's credit evaluation of the counterparty. Collateral held generally consists of certificates of deposit, share accounts, automobiles and real estate.

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

Financial instruments with concentration of credit risk: The Credit Union's lending activity is with its members as previously described in Note 1. The Credit Union's policy is to obtain collateral whenever necessary.

A substantial portion of the cash equivalents portfolio is comprised of deposits in Catalyst Corporate Federal Credit Union. As of December 31, 2018, the deposit exceeds the insured amount by approximately $1,170,000 for Catalyst Corporate Federal Credit Union.

NOTE 9: RELATED-PARTY TRANSACTIONS

In the normal course of business, the Credit Union extends credit to directors, supervisory committee members and executive officers. The aggregate loans as of December 31, 2018 and 2017 amounted to approximately $1,770,000 and $2,480,000, respectively. Deposits from those related parties as of December 31, 2018 and 2017 amounted to approximately $350,000 and $360,000, respectively.

Bourns, Inc. provided support and services, including personnel and related benefit costs, office space, data processing, and various other operating expenses for the benefit of the members of Bourns Employees Federal Credit Union. The Credit Union reimburses these costs. Any unpaid amount are recorded as part of liabilities as of December 31, 2018.

NOTE 10: RETIREMENT PLAN

401(k) Retirement plan: The Credit Union has a 401(k) retirement plan through Bourns, Inc., for all employees who have met both the tenure and minimum age requirements specified in the plan. The Credit Union contributions are based on a percentage of employee compensation and totaled $20,378 and $18,715 for the years ended December 31, 2018 and 2017, respectively.

NOTE 11: REGULATORY CAPITAL

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

Quantitative measures established by regulation to ensure capital adequacy require the Credit Union to maintain minimum amount and ratios (set forth in the table below) of net worth (as defined in the regulations) to assets (as defined). Credit Unions are also required to calculate a Risk-Based Net Worth Requirement (RBNWR), which establishes whether or not the Credit Union will be considered “complex” under the regulatory framework. The Credit Union’s RBNWR ratio as calculated by the NCUA as of December 31, 2018 is 5.99%. The minimum ratio to be considered complex under the regulatory framework is 6%. Management believes that as of December 31, 2018, the Credit Union meets all capital adequacy requirements to which it is subject.

NOTE 11: REGULATORY CAPITAL - *continued*

As of December 31, 2018, the most recent call reporting period, NCUA categorized the Credit Union as "well-capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well-capitalized," the Credit Union must maintain a minimum net worth ratio of 7% of assets and meet any applicable RBNWR. There are no conditions or events since that notification that Management believes have changed the Credit Union's category.

The Credit Union's actual capital amounts and ratios as of December 31, 2018 are also presented in the table, as follows:

Actual		For Capital Adequacy Purposes		To be Well-Capitalized per Prompt Corrective Action Provisions	
Amount	Ratio	Amount	Ratio	Amount	Ratio
$ 7,500,478	15.2%	$ 2,953,310	6.0%	$ 3,445,528	7.0%

The calculations above are made without including other comprehensive income.

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

NOTE 12: MORTGAGE SERVICING RIGHTS

Mortgage loans serviced for Federal National Mortgage Association (FNMA or Fannie Mae) are not included in the accompanying statements of financial condition. The unpaid principal balance of the loans being serviced was $109,319,950 and $83,729,888 as of December 31, 2018 and 2017, respectively.

A summary of the changes in the balance of mortgage servicing rights for the period ended December 31, 2018 and 2017 is as follows:

	December 31, 2018	December 31, 2017
Balance, beginning of year	$ 1,030,741	$ 538,877
Servicing assets recognized during the year	490,371	702,242
Amortization of servicing assets	(272,840)	(210,378)
Balance, end of year	$ 1,248,272	$ 1,030,741

NOTE 13: ACQUISITION AND MERGER

In February 2017, Bourns Employees Federal Credit Union acquired the assets and assumed the liabilities of Bakery Employees Credit Union. The fair value of assets acquired from Bakery Employees Credit Union totaled to $6.98 million.

Non-cash investing activity due to acquisition with Bakery Employees Credit Union is as follows:

Fair value of investments, property, and other assets acquired	3,241,018
Fair value of loans receivable acquired	1,608,746
Fair value of members' share accounts assumed	6,305,941
Fair value of liabilities assumed	83,256

NOTE 14: SUBSEQUENT EVENTS

Bourns Employees Federal Credit Union acquired the assets and assumed the liabilities of Colton Federal Credit Union effective February 28, 2019.

In February 2019, the National Credit Union Administration (NCUA) Board unanimously approved another share insurance distribution of $160 million to eligible federally insured credit unions. The distribution will be paid out in the second quarter of 2019. The Credit Union will receive approximately $6,700.

The Credit Union has evaluated subsequent events through March 29, 2019, which is the date the financial statements were available to be issued.

Board of Directors and Supervisory Committee
Bourns Employees Federal Credit Union
Riverside, California

INDEPENDENT AUDITOR'S REPORT ON SUPPLEMENTARY INFORMATION

We have audited the financial statements of Bourns Employees Federal Credit Union as of and for the year ended December 31, 2018, and our report thereon dated March 29, 2019, which expressed an unmodified opinion on those financial statements, appears on page AFS-1 and page AFS-2. Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying information listed below is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of Management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the accompanying information presented herein is fairly stated in all material respects in relation to the financial statements taken as a whole.

Schedule of Other General and Administrative Expenses

Summary of Reclassifying and Adjusting Entries

Review of Financial Trends

RICHARDS & ASSOCIATES
Certified Public Accountants

Michael E. Richards, CPA

Yorba Linda, California
March 29, 2019

BOURNS EMPLOYEES FEDERAL CREDIT UNION

SCHEDULE OF OTHER GENERAL AND ADMINISTRATIVE EXPENSES

Years ended December 31, 2018 and 2017

	2018	2017
Loan servicing	$ 194,267	$ 181,144
Office occupancy	61,886	57,100
Outsourced services	47,302	43,300
Education and promotion	31,932	44,171
Travel and conference	22,315	30,927
Association dues	12,718	12,139
Regulatory supervision	12,458	8,734
Members' insurance	271	480
Miscellaneous expenses	15,713	21,959
	$ 398,862	$ 399,954

This schedule is supplemental information only.

BOURNS EMPLOYEES FEDERAL CREDIT UNION

SUMMARY OF RECLASSIFYING AND ADJUSTING ENTRIES

For the year ended December 31, 2018

	DEBIT	CREDIT
RECLASSIFYING ENTRY 1		
Undivided earnings	$ 497	
Equity acquired through merger		$ 497

To reclassify the net income from Bakery Employees Federal Credit Union in February 2017.

	DEBIT	CREDIT
RECLASSIFYING ENTRY 2		
Other income	$ 6,042	
Income from investments		$ 6,042

To reclassify income from credit union service organization.

	DEBIT	CREDIT
RECLASSIFYING ENTRY 3		
Investments	$ 89,084	
Other assets		$ 89,084

To reclassify investments in credit union service organizations.

	DEBIT	CREDIT
RECLASSIFYING ENTRY 4		
Other assets	$ 326	
Loans receivable		$ 326

To reclassify cash advance in process as of December 31, 2018.

This schedule is supplemental information only.

SUMMARY OF RECLASSIFYING AND ADJUSTING ENTRIES - *continued*

For the year ended December 31, 2018

	DEBIT	CREDIT
RECLASSIFYING ENTRY 5		
Share insurance deposit	$ 30,000	
Other assets		$ 30,000

To reclassify share insurance deposit balance at American Share Insurance as of December 31, 2018.

	DEBIT	CREDIT
RECLASSIFYING ENTRY 6		
Loans receivable	$ 3,270	
Members' share and savings accounts		$ 3,270

To reclassify negative shares to loans receivable.

	DEBIT	CREDIT
RECLASSIFYING ENTRY 7		
Other non-operating income	$ 490,371	
Gain on mortgage servicing assets		$ 490,371

To reclassify the gain on servicing rights.

	DEBIT	CREDIT
ADJUSTING ENTRY 1		
Members' insurance	$ 17,612	
Undivided earnings		$ 17,612

To reverse the adjustment to accrued Temporary Corporate Credit Union stabilization expense as of December 31, 2017.

This schedule is supplemental information only.

SUMMARY OF RECLASSIFYING AND ADJUSTING ENTRIES - *continued*

For the year ended December 31, 2018

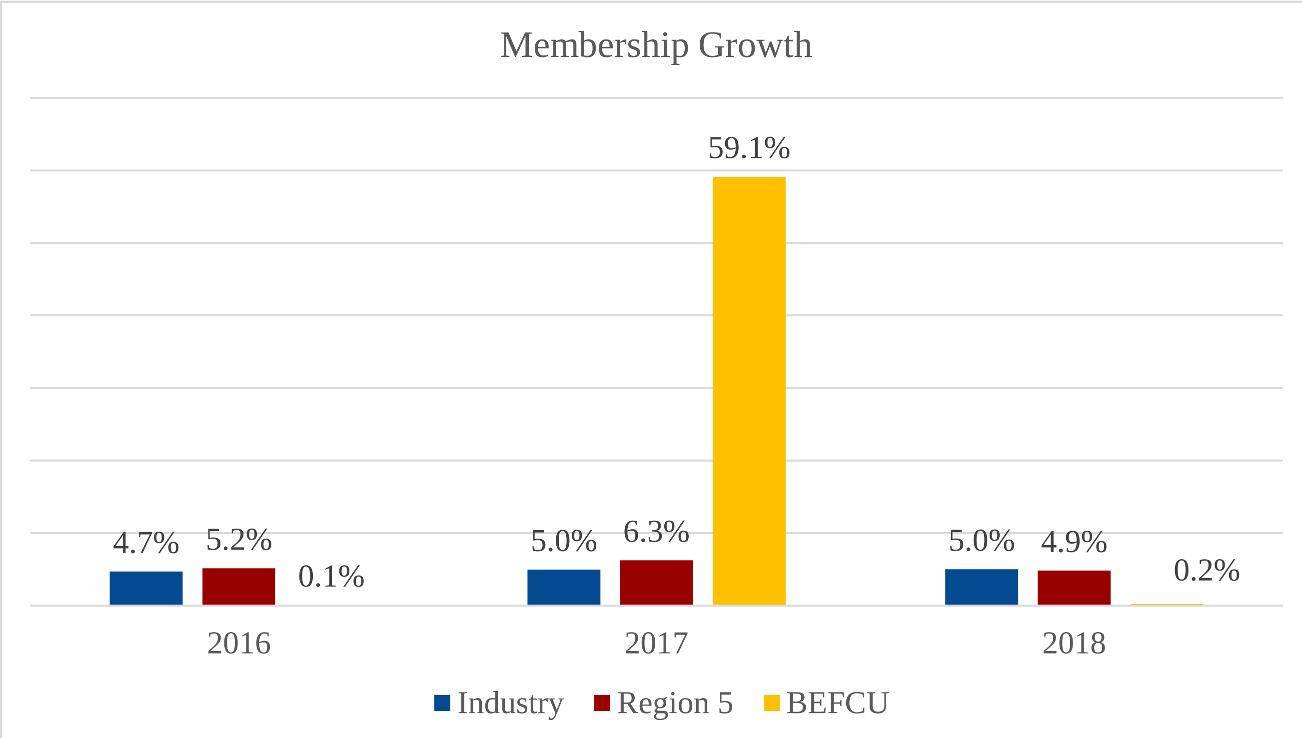
ADJUSTING ENTRY 2

	DEBIT	CREDIT
Accrued expenses	$ 17,612	
Members' insurance		$ 17,612

To reverse the accrual for regulatory assessment as of December 31, 2018.

This schedule is supplemental information only.

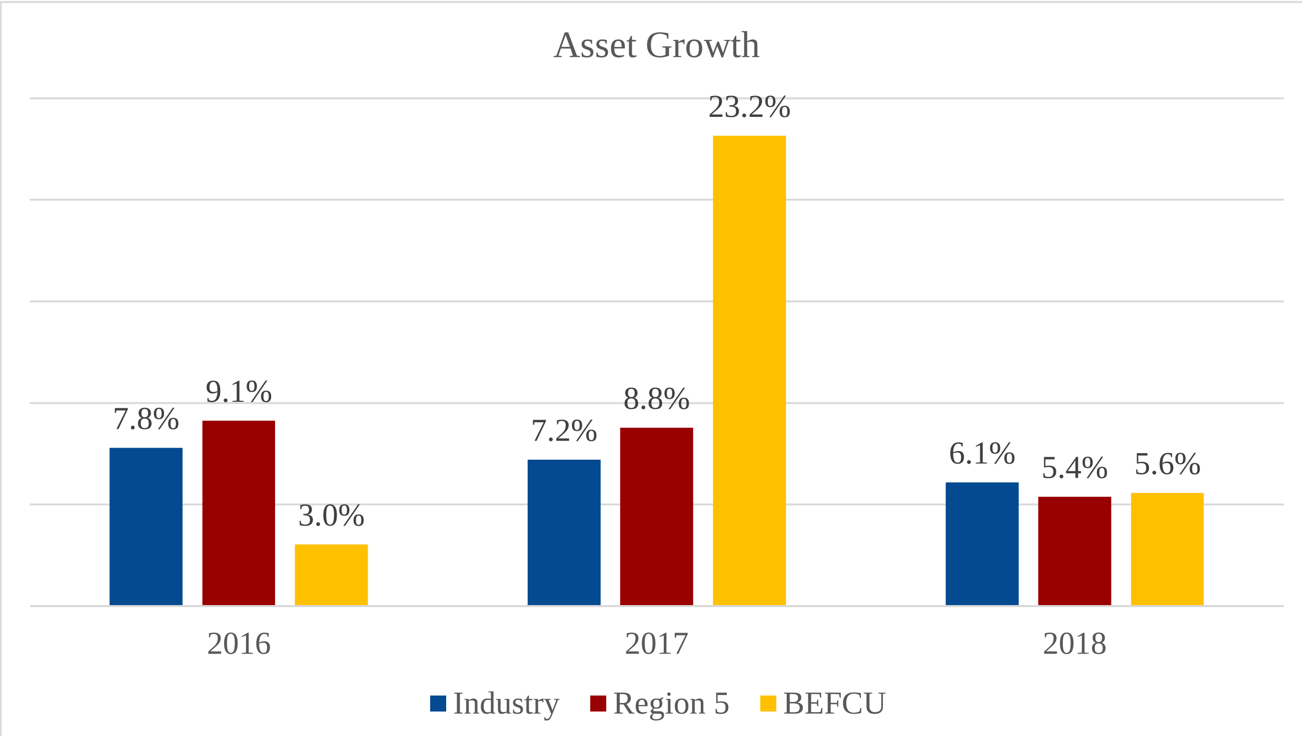
Bourns Employees Federal Credit Union
Financial Trends 2016 through 2018



Accountant's Comments

Membership growth is the result of implementing effective business strategies in the Credit Union's market place. Member growth strategies are driven by the board's philosophy towards service levels, delivery channels, product pricing, and breadth of services offered. From a strategic planning perspective, membership growth is where the rubber meets the road.

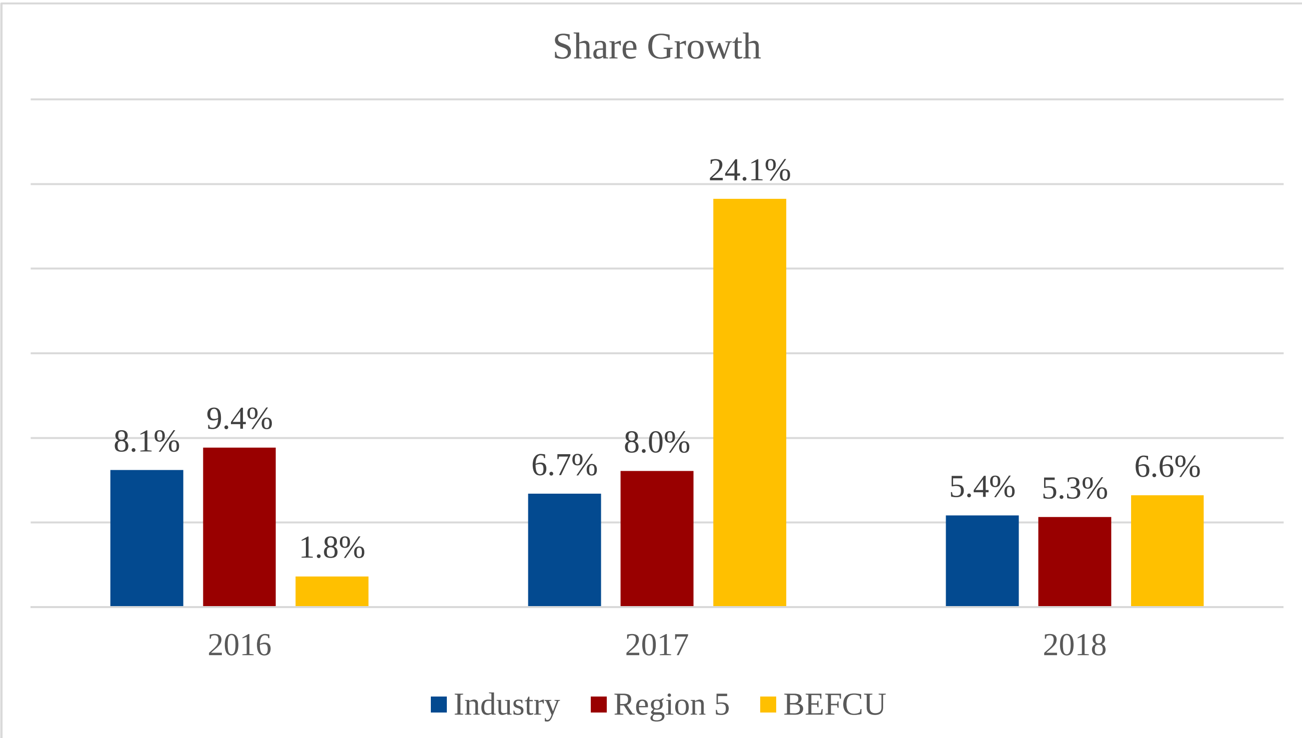
Bourns Employees Federal Credit Union
Financial Trends 2016 through 2018



Accountant's Comments

A credit union’s asset growth is affected by both internal and external factors. The external factors include the state of the economy, and the make-up and size of the credit union’s field of membership. The internal factors include the quality of member service, the menu of products available, and the credit union’s pricing philosophy.

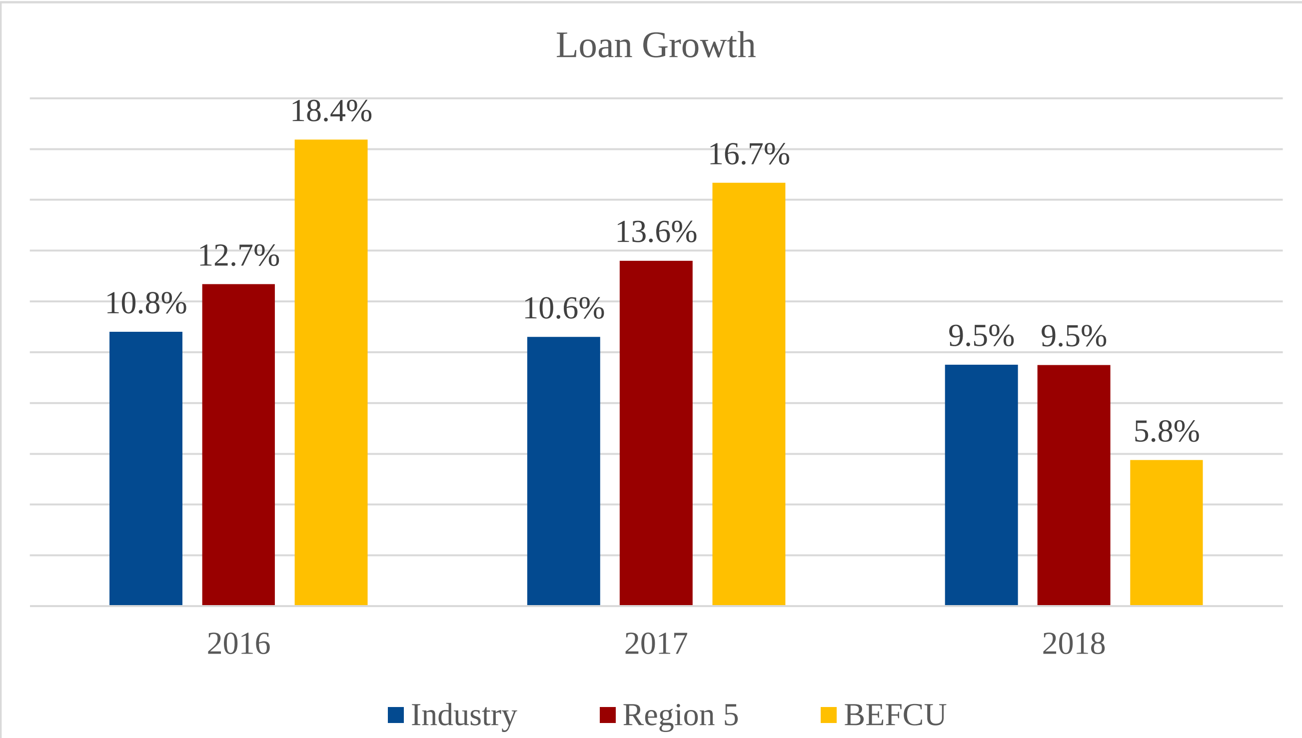
Bourns Employees Federal Credit Union
Financial Trends 2016 through 2018



Accountant's Comments

This ratio impacts more than one risk area. It provides a general view of the credit union's growth in shares for the cycle and may help to assess interest rate risk. Rapid growth in shares may indicate inappropriate pricing and increased volatility in the balance sheet. Share growth also reflects a credit union's risk management practices, and is a factor in assessment of strategic risk and planning. Share growth that outpaces the ability to generate sufficient net income (a primary earnings ingredient is loan interest income) reduces the overall strength of the credit union's net worth.

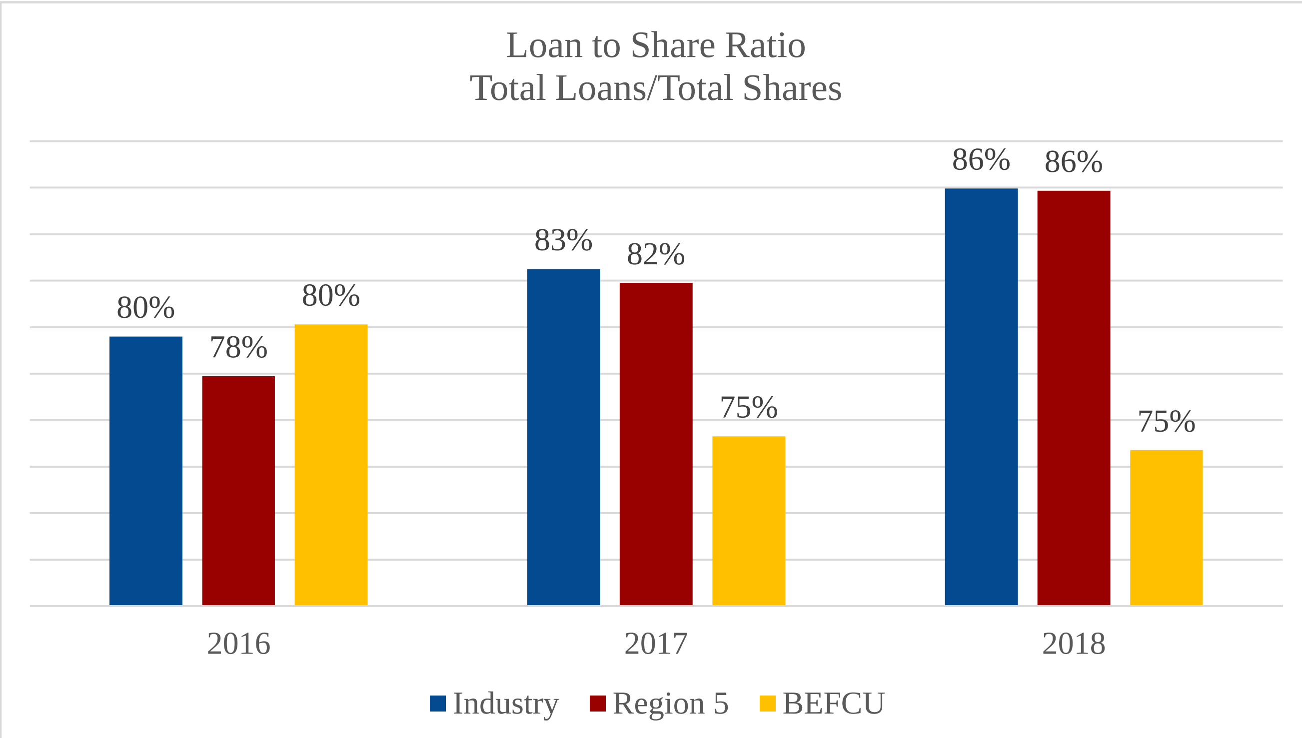
Bourns Employees Federal Credit Union
Financial Trends 2016 through 2018



Accountant's Comments

Loan growth is driven by several factors, including the state of the economy, membership demographics, the level of risk the credit union is willing to manage, and the credit union’s ability to gain market share. The overall market for loans is influenced by the membership’s confidence in their ability to manage debt. The demographic factors that influence loan growth include the number of borrowing age members, how affluent the membership is, and their cultural attitudes towards debt and borrowing. The credit union’s ability to penetrate its potential loan market through marketing, product development, sales culture development, and the use of multiple delivery channels are all reflected in this ratio.

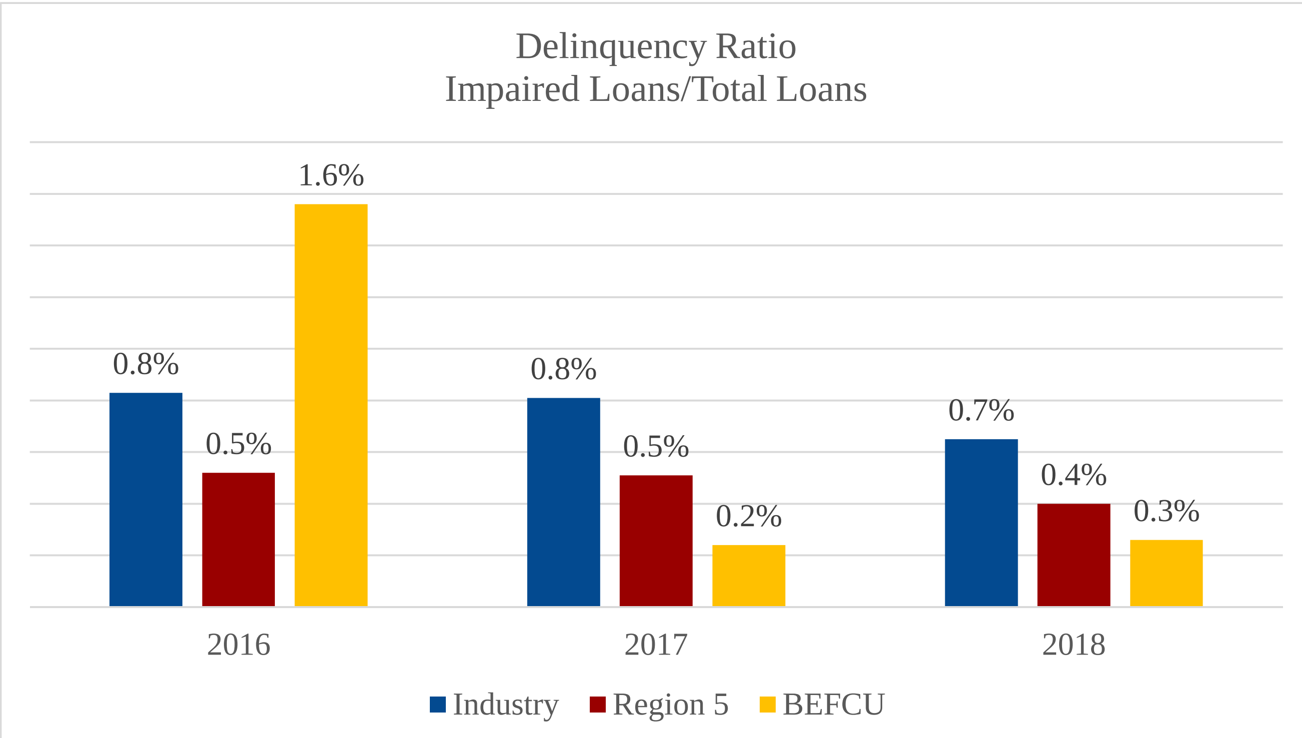
Bourns Employees Federal Credit Union
Financial Trends 2016 through 2018



Accountant's Comments

The loan-to-share ratio is driven by the credit union's loan and deposit acquisition performance. Most credit unions concentrate on building the loan portfolio while focusing less on deposits, unless liquidity is an issue. In general, loan growth can be influenced more by the credit union's operations (sales culture, marketing, product development, risk management, etc.) than deposit growth. Deposit growth is generally influenced more by non-operational factors like membership demographics than by operational factors. In general, a higher ratio indicates greater profitability.

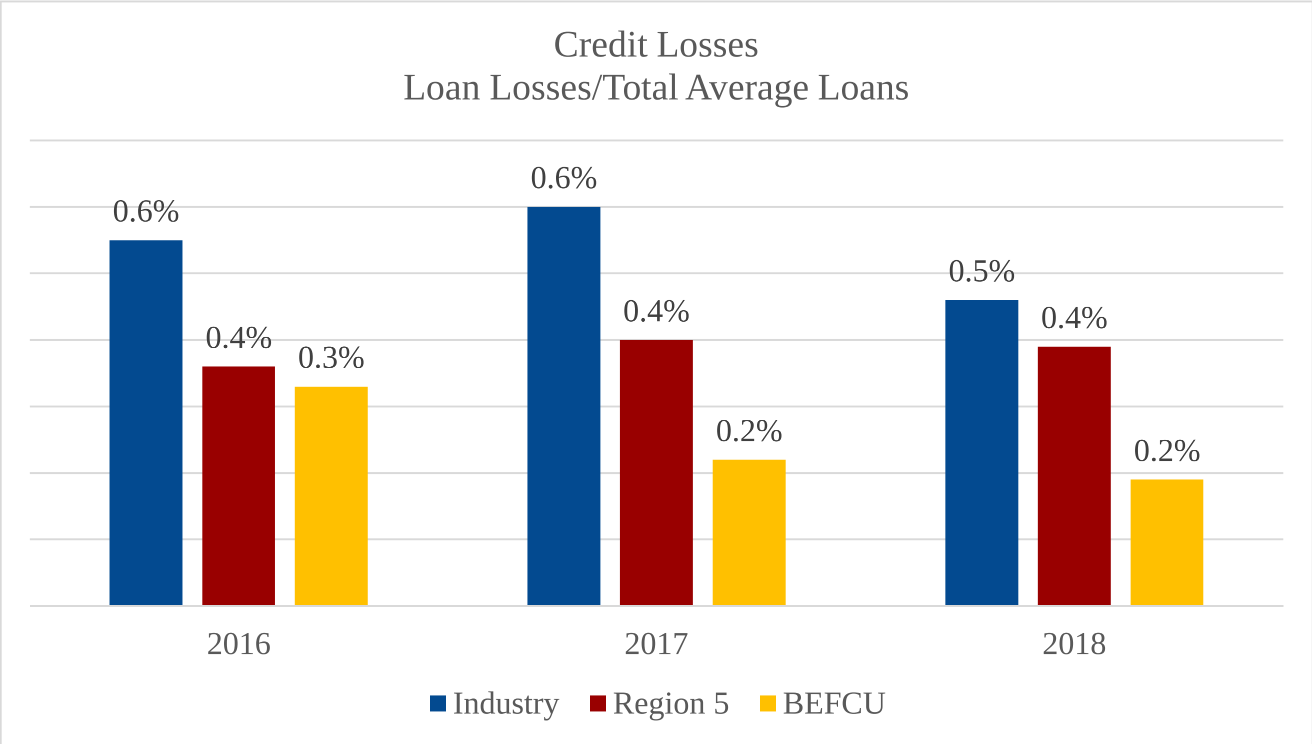
Bourns Employees Federal Credit Union
Financial Trends 2016 through 2018



Accountant's Comments

This Asset Quality ratio measures delinquent loans in relation to total loans. This ratio is an indicator of the effectiveness of delinquency control and quality of loans held in portfolio. A high ratio in relation to regional and national averages indicates the credit union may have higher loan and lease loss requirements relative to other credit unions.

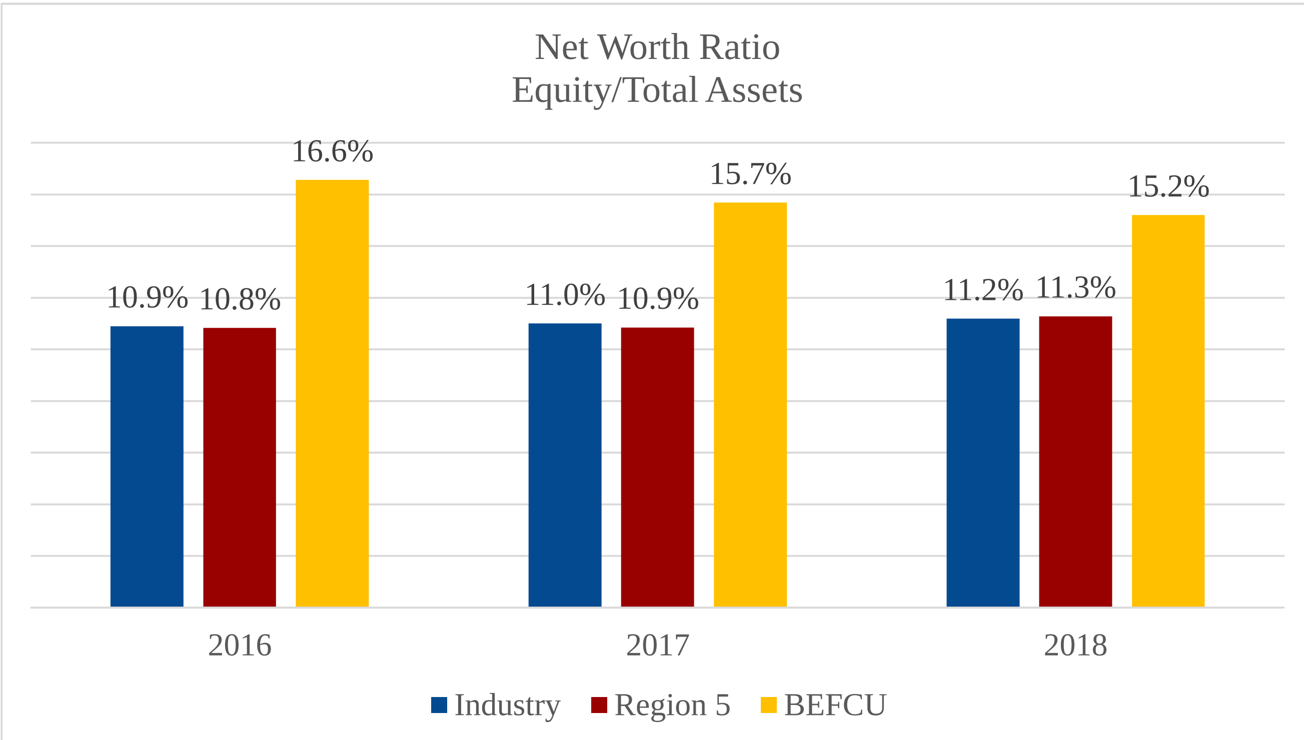
Bourns Employees Federal Credit Union
Financial Trends 2016 through 2018



Accountant's Comments

This Asset Quality ratio measures net charge-offs in relation to average loans. Net charge-offs are an important indicator of the effectiveness of lending and collection practices. A high ratio in relation regional and national averages may indicate a higher level of uncollectible loans relative to other credit unions.

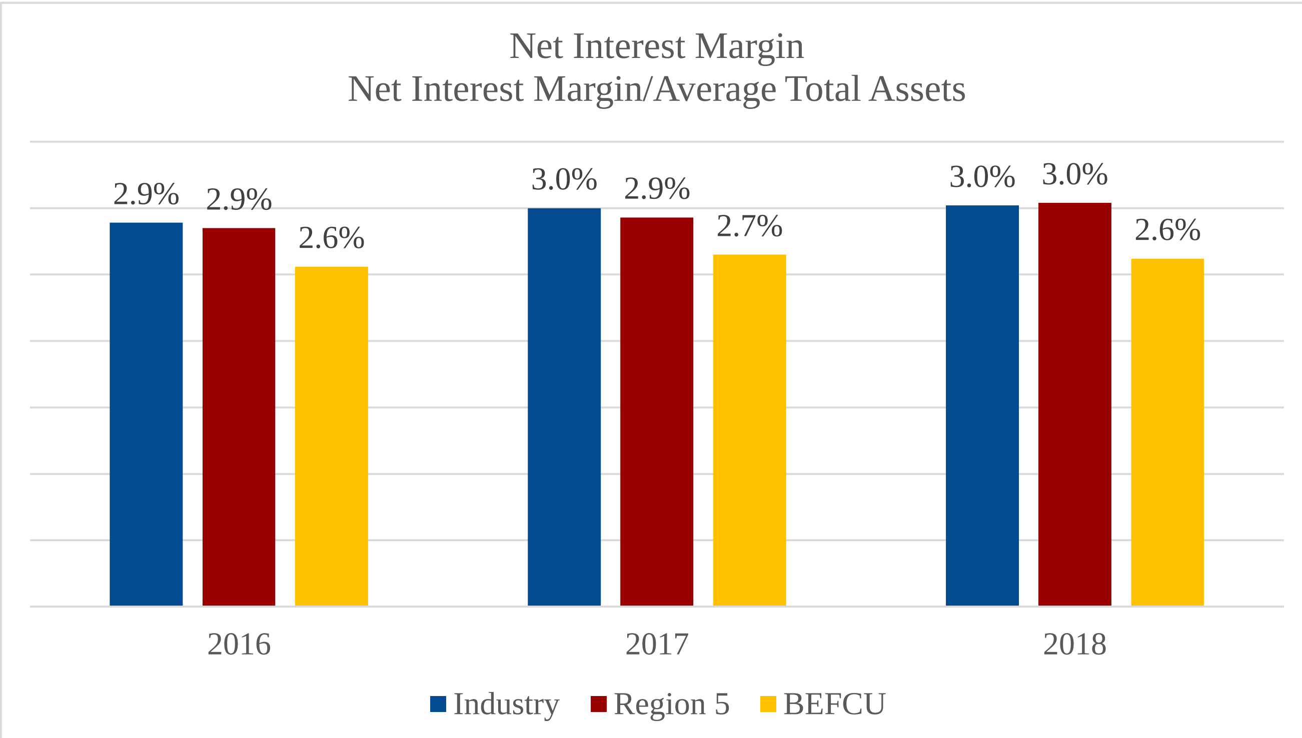
Bourns Employees Federal Credit Union
Financial Trends 2016 through 2018



Accountant's Comments

This Capital Adequacy ratio measures net worth in relation to total assets. Net worth cushions fluctuations in earnings, supports growth, and provides protection against insolvency. The rate of net worth growth should be commensurate with the levels of risk and asset growth.

Bourns Employees Federal Credit Union
Financial Trends 2016 through 2018

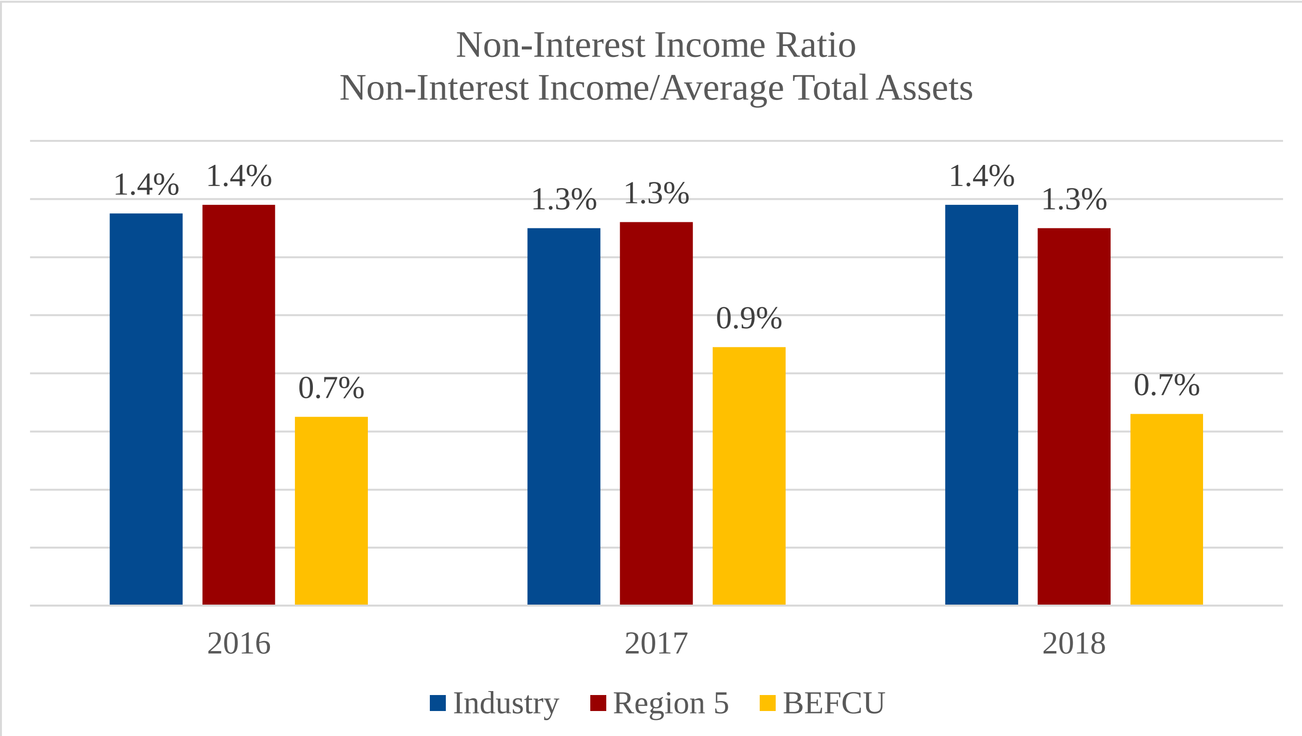


Accountant's Comments

The measure is the result of the credit union's execution of its lending, investing, and liquidity strategies. The credit union's ability to manage its spread is a critical component in managing this metric. For example, appropriately pricing loan products (via risk-priced loans) or deposit products (through a clear differentiation between rate sensitive and non-rate sensitive products) significantly enhances the organization's flexibility in managing the margin.

Credit unions with lower operating expense levels or strong non-interest income will be able to sustain more competitive loan and deposit pricing strategies. Credit unions with higher expenses, loan losses, or lower non-interest income levels will need to maintain higher net interest margins.

Bourns Employees Federal Credit Union
Financial Trends 2016 through 2018

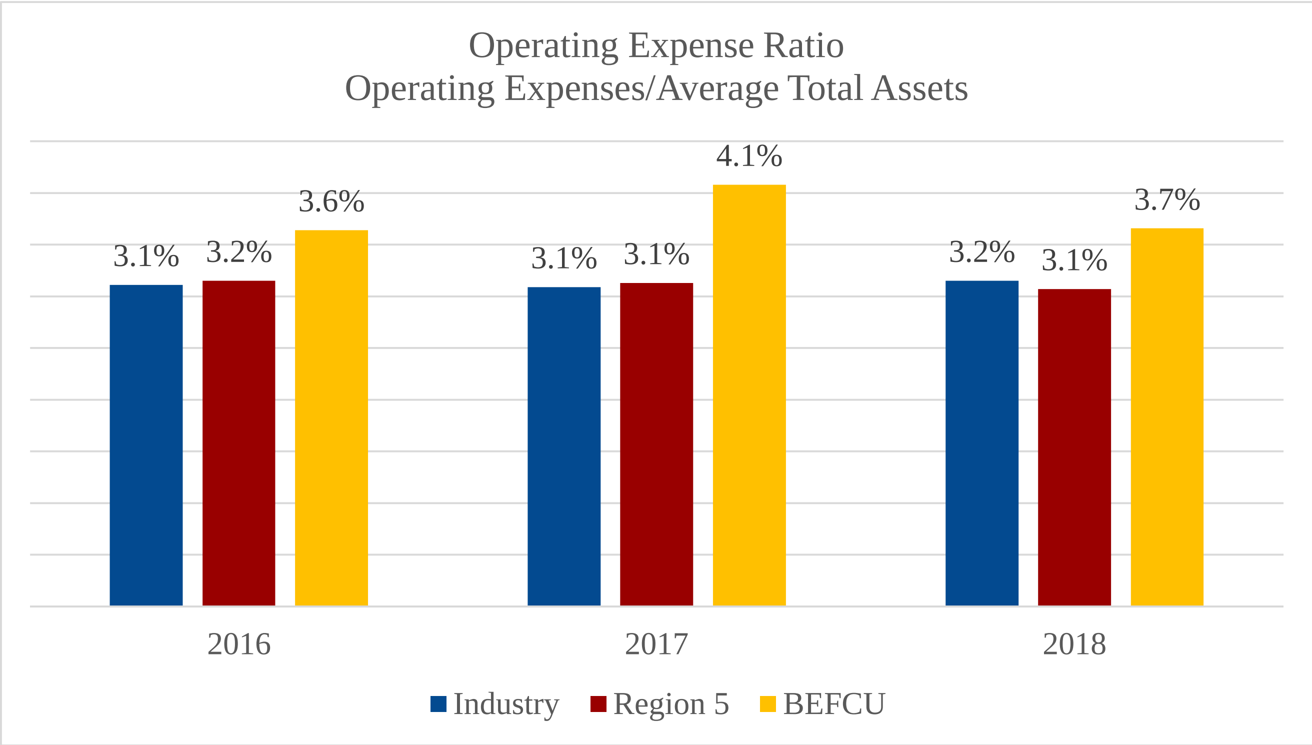


Accountant's Comments

This ratio measures the amount of non-interest income the credit union generates as a percentage of average assets. The higher the number, the more income is being generated by sources other than asset-based products. Analyzing non-interest income as a percentage of assets removes the variations that exist when comparing the ratio to total income (e.g., viewing by assets removes the impact of a weak loan-to-asset ratio). Non-interest income factors that impact the ratio generally fall into two major categories.

The first is income generated directly from members in the form of fees. The second is income generated indirectly from members or other aspects of the credit union's operations (e.g., interchange income from credit and check cards). The rate of asset growth is the most impactful variable on the ratio, although strategies for non-interest income play a part as well. Rapid asset growth will depress the ratio, while slow or stagnant asset growth will inflate the ratio.

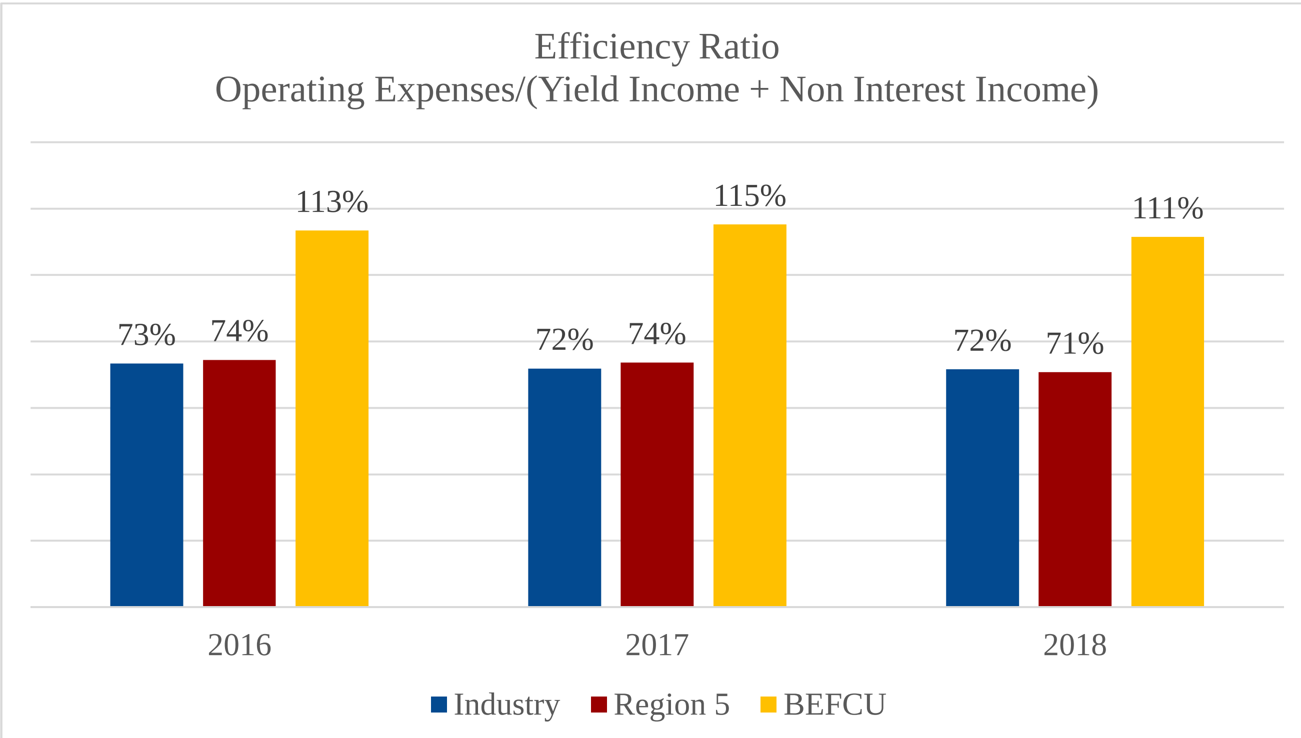
Bourns Employees Federal Credit Union
Financial Trends 2016 through 2018



Accountant's Comments

The operating expense ratio reflects both the operating efficiency and the operating strategy of a credit union. The breadth of a credit union's product and service line will also have an impact on this ratio. Managing expenses more efficiently can have a significant impact on a credit union's competitiveness and the value it creates for members. In comparing expenses to assets, this ratio underscores the idea that a larger balance sheet is a result of a larger operation that requires greater resources. The ratio can be compared to the operating expense to income ratio, which can show larger swings due to the impact of interest rate changes on total income. Overall, credit unions are operated very efficiently.

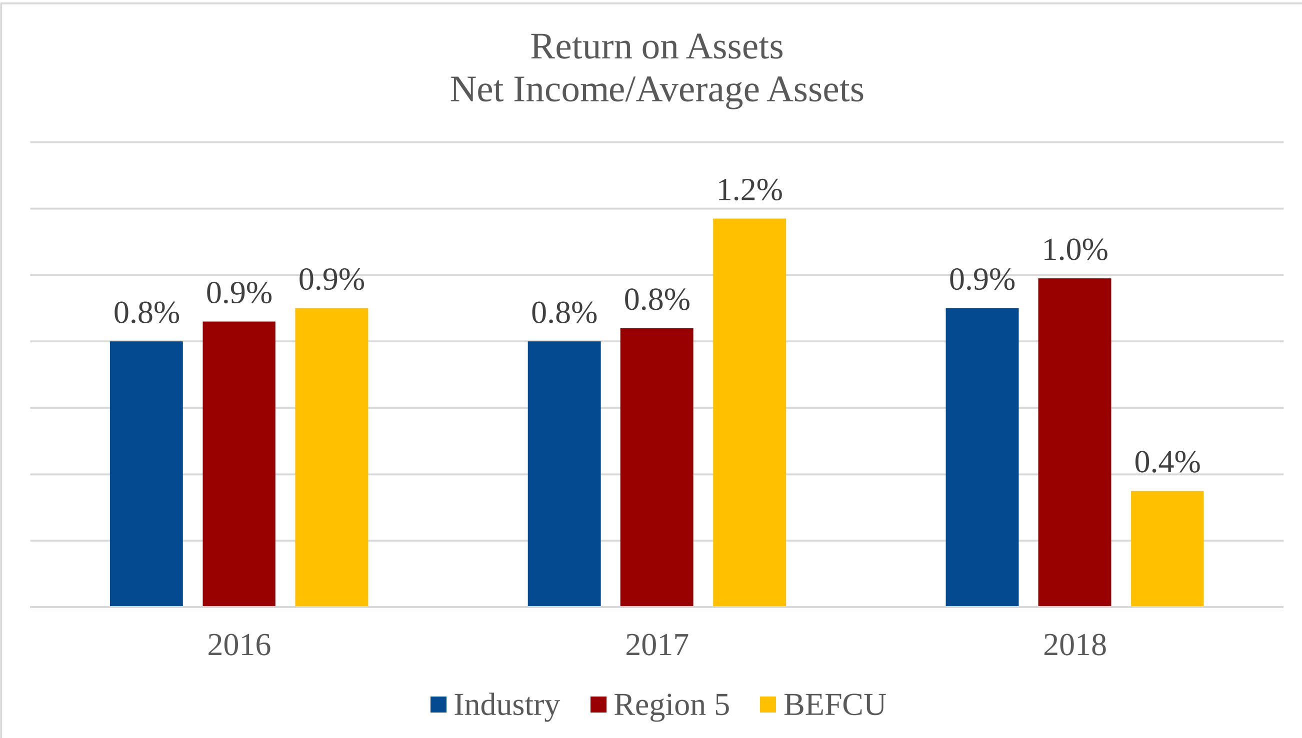
Bourns Employees Federal Credit Union
Financial Trends 2016 through 2018



Accountant's Comments

The lower the efficiency ratio, the better. A high or rising efficiency ratio means that the credit union is losing a larger share of its income to overhead expenses. A low efficiency ratio means that operating expenses are a smaller percentage of income. In general terms, the efficiency ratio can be interpreted as how much does it cost the credit union to create $1 of revenue. The efficiency ratio can fluctuate over time, influenced by the interest rate environment since income is generally more sensitive to changes in interest rates than expenses are. In theory, credit unions with higher ratios of non-interest income to total income should see less fluctuation in the efficiency ratio than credit unions with little fee income.

Bourns Employees Federal Credit Union
Financial Trends 2016 through 2018



Accountant's Comments

Return on Assets (ROA) is an important gauge of a credit union's profitability. It shows how efficiently management is running the credit union by revealing how much income is generated for each dollar of assets deployed. In general, a high ROA relative to state and national averages reflects management's success at utilizing its assets to generate income. Credit unions, however, should view ROA in light of their institution's distinct strategy. For example, if a credit union passes along potential profits to members (e.g., no fees, high deposit rates, low lending rates), then its strategy might result in a lower ROA relative to other credit unions.