FIGFCU GIVES BACK

2012 ANNUAL REPORT

Farmers Insurance Group
Federal Credit Union

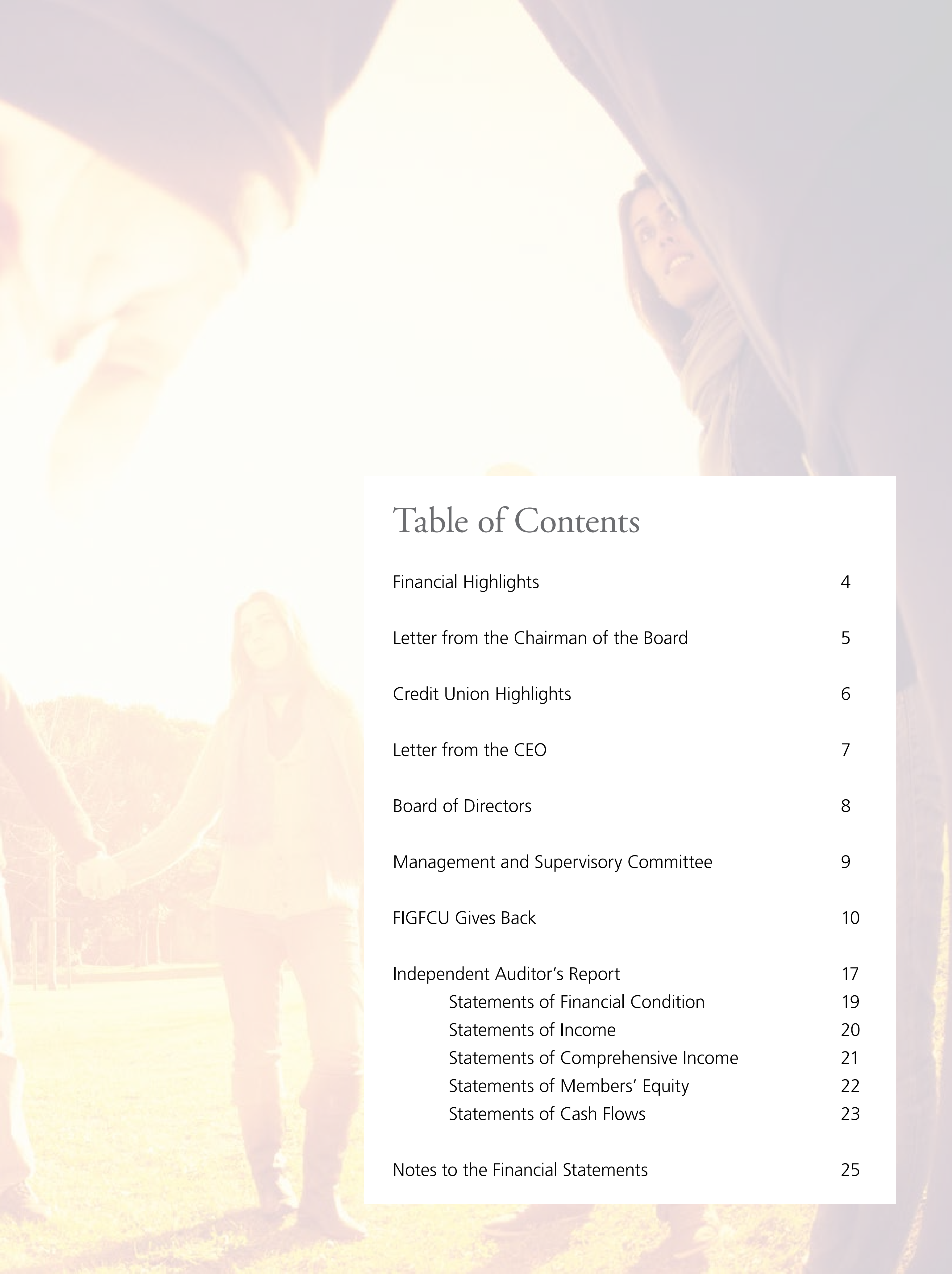
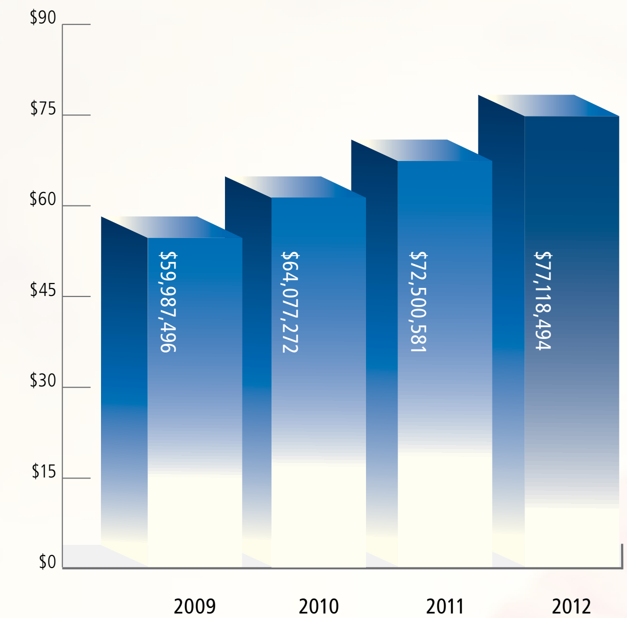


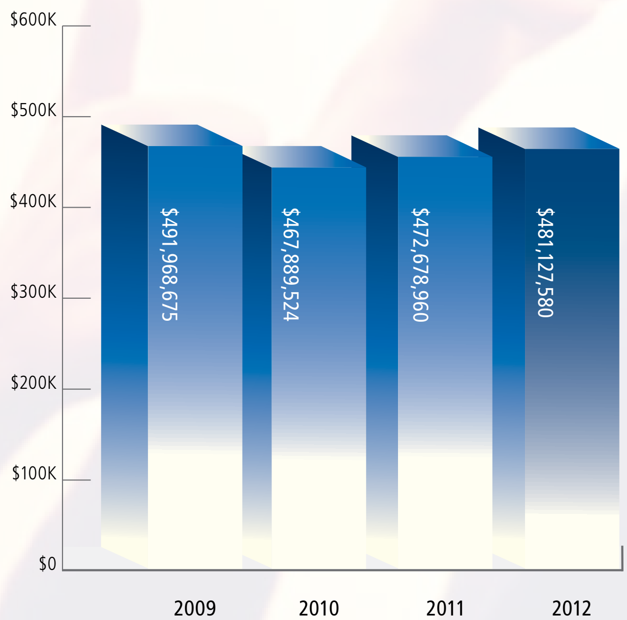
Table of Contents

Financial Highlights 2009-2012

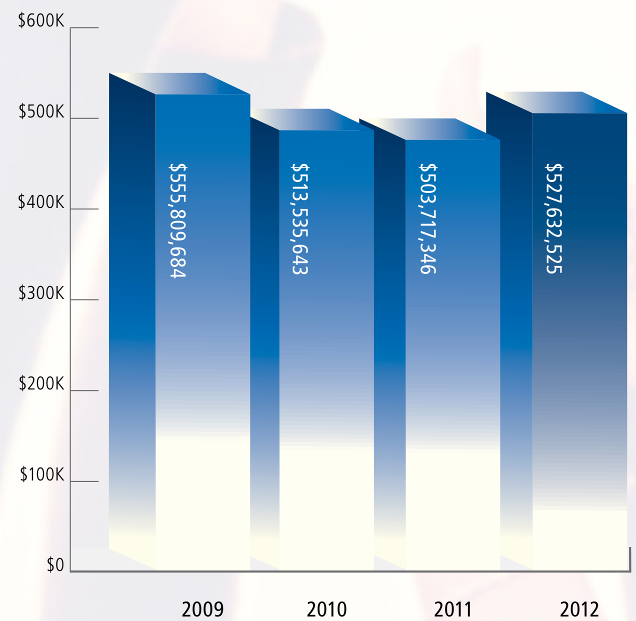


Retained Earnings

Net Income



Total Net Loans



Member Shares

Letter from the Chairman of the Board

Dear Valued Farmers Insurance Group Federal Credit Union Members,

Another year has gone by and in many ways, not much has changed. The same president has remained in office, and a still-divided Congress was enmeshed in yet another year of "gridlock" politics, leading to the much-maligned event referred to as "Sequestration." So, the issues that have impacted the economy for years now, particularly the European Union's financial struggles, the domestic housing crisis, deficit spending and elevated levels of unemployment, have continued to be obstacles for a strong economic recovery.

In spite of this not-so-rosy economic environment, your Credit Union has met these challenges head on, and experienced another successful year in 2012 with impressive results.

At the close of the year, assets stood at $610,272,000, while delinquency continued to drop, ending the year at a low 1.3%, down from 2.7% one year prior. FIGFCU saw net income of $4.6 million, bringing our year-end net worth to over $77 million. As a result, the Credit Union's net worth as a percent of assets at the end of 2012 was a robust 12.6%, making us one of the best capitalized credit unions in our industry.

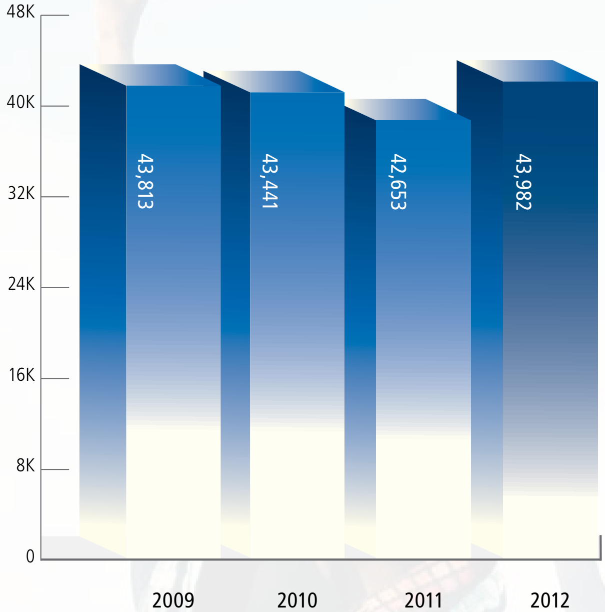
In a year when other financial institutions continued to bolster their bottom lines and adjust to the economic circumstances by inflating existing fees and devising ever new ones, your Credit Union made a decision in the opposite direction by returning, rather than diminishing, value to our member-owners. Rebates on loans, low-rate loan specials and even an end-of-year membership bonus, are a few examples of how FIGFCU returned over $1.25 million to our loyal members in 2012.

Projections for 2013 point to a continuation of the conditions that have been prevalent over the last few years – sub-optimal economic growth, lingering unemployment, and historically very low interest rates. But even against the backdrop of these conditions, FIGFCU is committed to providing a wide range of products and services tailored to the needs of our specific membership, for the continuing betterment of your financial lives. We will press forward with efforts to reach more members, deliver additional products and services to existing members, and grow our lending services over the next year, all the while maintaining the high level of service that you have come to expect from us.

On behalf of Farmers Insurance Group Federal Credit Union, I wish to personally thank you for your continued trust in our organization. With your support, we look forward to the opportunities that lie ahead and for continued success in 2013.

Laszlo G. Heredy, Chairman of the Board

Credit Union Highlights 2009-2012



Total Members

Total Assets

Letter from the CEO

Dear Members,

What differentiates our Credit Union's member value proposition from that of a bank, or most any other credit union? Before I answer that, let me quickly define what I mean by our value proposition. In a nutshell, it means all the various reasons our members choose to keep doing business with us, as opposed to some other government-insured financial institution.

First of all, as about 98% of our members and potential members have a direct relationship, many by family relations, to Farmers, we principally exist to serve Farmers. We succeed there. I am very proud to tell you that your Credit Union serves as a critically important and viable financial intermediary for you, and that we enhance your overall Farmers employment or agency experience. That is simply a fundamental part of who and what we are; no other bank or credit union can validly make that assertion. We do. We understand what's going on in the Farmers culture better than any bank does, and we understand our vital role in those myriad relationships that help make Farmers successful. No other financial institution exists to help make Farmers stronger. We do.

Second, and third, and beyond, lies our highly competitive suite of products and services. We seek to, and do, enhance our member/owners' financial lives. We manage our balance sheet under the primary guiding light of minimizing our bottom line, NOT maximizing our profit. Do you know of any bank whose strategic mission is articulated as minimizing its bottom line? I doubt it. Now, we minimize our desired profitability, yet still build our reserves year over year, and in the process, we maximize the return of value to you . In fact, I hope you took advantage of your fair share of the $1.25 million return of value programs and specials offered in 2012. We could have retained that $1.25 million in our capital structure without upsetting you much, but we didn't. We returned it to you.

After all the very tangible reasons you choose to do business with us, such as pricing and convenience, come the real foundation of our business: service. We are retail, so we serve. We exist to serve our member/owners. Our first goal is to meet all our members' viable borrowing needs. We want your loan business! Our second goal is to attract your savings/investment funds. But again, the fabric, the very foundation of earning your loan business and your savings business, is our great service. Information gathered from our member surveys told us we succeeded there, too. In 2012, almost 89% of responses measuring service and member loyalty came back with either a good or excellent rating.

To wrap, these annual reports communicate our financial condition to you first and foremost. In this report, you can see that we continue to have an extremely sound net worth position. No hyperbole, just facts. If you have any questions about this 2012 Annual Report, please feel free to contact me personally. We just started our 78th year, and we are proud of our many accomplishments in 2012. It is through our relationships with you and your loyal support, that we will continue to serve the Farmers family for another 77 years.

Mark Herter

Mark Herter, President/CEO

Board of Directors

Laszlo Heredy
Retired

Frank Ceglar
Executive Vice President and
General Counsel

Ed McMahan
District Manager, Phoenix, AZ

Michael Ashe
Agent, Las Vegas, NV

Marilyn Huntamer
Agent, San Diego, CA

Andy Reser
Senior Vice President,
Head of Agency Management

Kenneth Carroll
Retired

Scott Lindquist
Executive Vice President and
Chief Financial Officer

Jim Snikeris
Vice President,
Austin ServicePoint

Management Team

Harland Bengs
Chief Financial Officer

Yusef Mustafa
Chief Information Officer

Laura Campbell
Executive Vice President

Brian Leonard
Chief Lending Officer

Merk Herter
President/CEO

Kathy Chicas
Vice President, Operations

Beth Rodgers
Chief Marketing Officer

SUPERVISORY COMMITTEE

Andy Purl, Chairman, Senior Audit Consultant

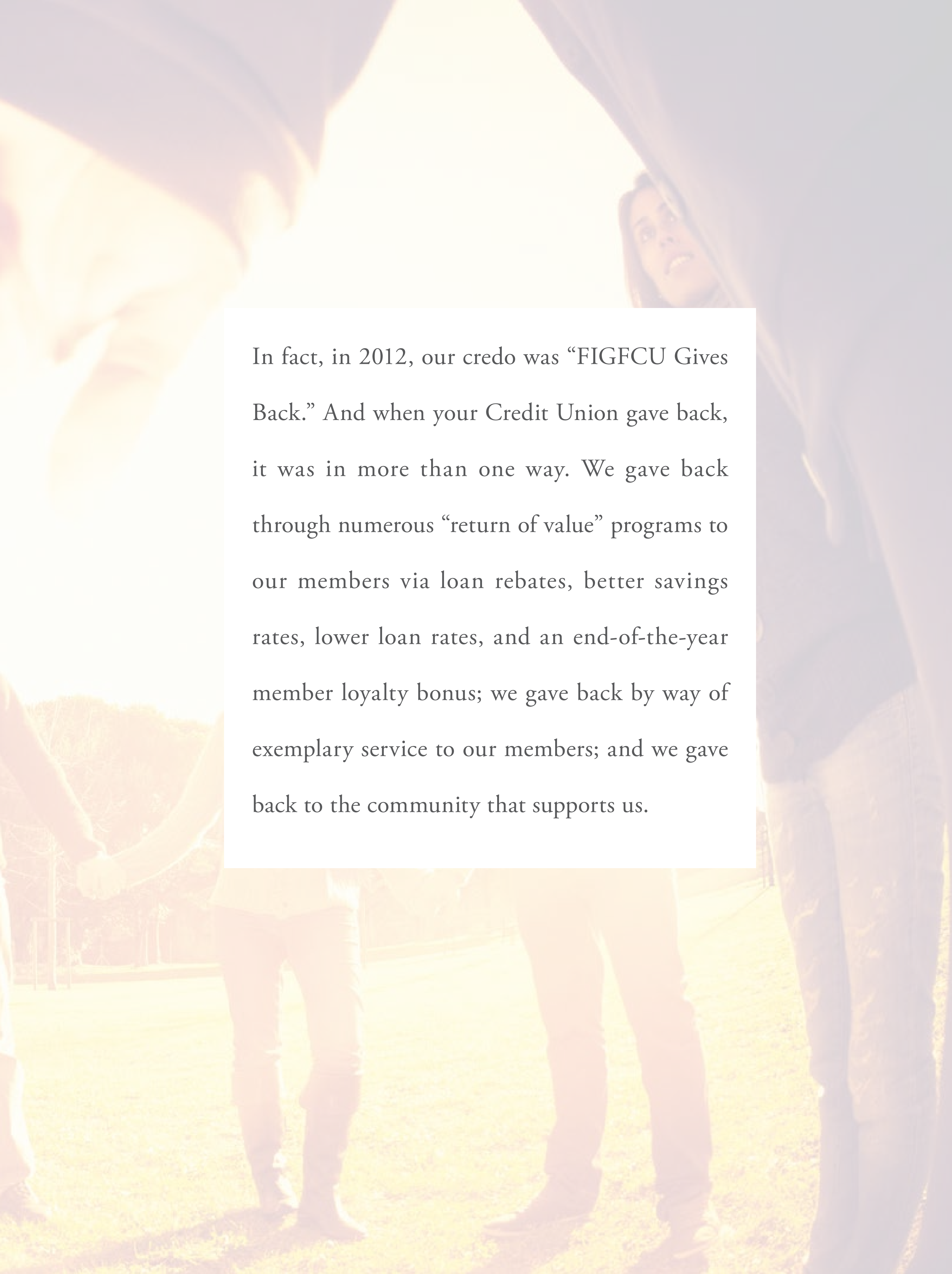
Karen Jenkins, Head of Distribution Compliance

Lewis Williams, Head of Farmers IT Finance

Rudolfo Trevino, Chief Compliance Officer

FIGFCU GIVES BACK

Last year was another challenging year for the financial industry. But while the economy as a whole suffered, Farmers Insurance Group Federal Credit Union (FIGFCU) remained safe and sound.



In fact, in 2012, our credo was "FIGFCU Gives Back." And when your Credit Union gave back, it was in more than one way. We gave back through numerous "return of value" programs to our members via loan rebates, better savings rates, lower loan rates, and an end-of-the-year member loyalty bonus; we gave back by way of exemplary service to our members; and we gave back to the community that supports us.

RETURN of VALUE

FIGFCU has been the trusted financial partner of choice for Farmers agents and employees, and throughout the decades, we have sought ways to enhance the value provided to members by listening to your financial needs. Our products and services exist because of our members and their needs, and every day we continually strive to provide the best possible options.

In 2012, we launched our Round It Up program, to help you automatically save every time you use your debit card; Visa® Blue, a share-secured credit card, which gives you yet another option in our suite of credit card products; the introduction of Consolidation Student Loans, which makes it easier and more affordable for graduates to pay back multiple student loans; and Commercial Real Estate Contract Value Loans, for our agent-members, which allows agents to use contract value for the purchase or refinance of an agency office building.

We also enhanced the benefits of membership by introducing a deposit feature to our Mobile Banking app. Members now have the ability to conveniently make check deposits into their accounts by simply taking a picture with their smartphone.

Last year was highlighted by special programs, rebates and exclusive offers of which you took advantage. Among these were a 2% up-front auto loan rebate, a 1% up-front Agency Secured Loan rebate at the beginning of the year, and a 0% APR for 3 months on Agency Secured Loans in the summer, on top of our already affordable loan rates.

Other exceptional deals included 2.99% for 12 months on credit card balance transfers, 500 reward points for bringing over your Direct Deposit into an FIGFCU checking account, $450 towards an appraisal when closing a home loan, and 2.99% for 6 months on Home Equity Lines of Credit during the last quarter.

Certainly, the most popular in 2012 was our year-end "FIGFCU Gives Back More Than a Million Dollars!" program, where cash was awarded to loyal members, based on their relationship with the Credit Union. This membership bonus alone returned over $824,000 to our members!

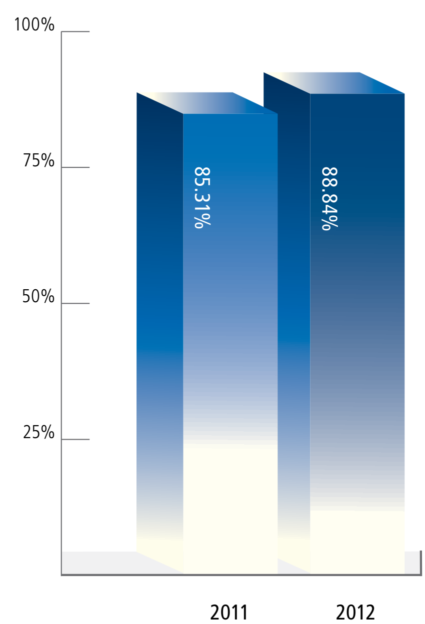
In 2012, your Credit Union gave back a total of over $1.25 million in "return of value" programs.

MEMBER SERVICE

We appreciate the trust that you put in the Credit Union to help you find the right financial solutions. While our strong financial position allowed us to give back to you, support worthy community causes and launch innovative products, a heavy focus still remained on providing exceptional service. With this in mind, every employee at FIGFCU is encouraged to use proactive thinking and initiative to optimize every member's experience with the Credit Union.

In 2012, FIGFCU continued to improve the level of service provided to our members by surpassing its Member Satisfaction Score goal of 88.13%, earning a score of 88.84%.

Our focus has remained consistent throughout the years — to build on our tradition of safety and soundness by providing first-rate service to our members. We remain passionately committed to this promise.



Member Satisfaction Score

SUPPORTING OUR COMMUNITY

The Credit Union and its employees are constantly motivated to give and make an impact in the communities where we live and work. Thanks to the generosity and fundraising efforts of FIGFCU staff and members, in 2012, over $64,000 was given to worthy causes – $37,000 was donated to the Farmers Family Fund, over $25,000 was donated to the March of Dimes, and over $2,800 was donated to the Children’s Miracle Network Hospitals.

2013 and BEYOND

Since our beginning in 1936, your Credit Union has supported the needs and dreams of its members. As we head into our 78th year, we have good reason to be proud.

Firmly standing at almost 44,000 members, with over $610 million in assets, our original mission remains as timely as it was in 1935 – we are helping our members achieve their financial goals. Whether it be a car, a home, a college education, agency growth or simply a better and more affordable way to bank, we have been and will continue to be the best financial services provider.

In the years ahead, we'll continue to expand the tools and resources available to our members to help them effectively manage their finances and support them in achieving their goals, in addition to welcoming more new members, by offering consumer-friendly alternatives not found at big banks. We look forward to continued success – as we continue to invest in each other – through 2013 and beyond.

FIGFCU GIVES BACK

Orth, Chakler, Murnane and Company, CPAs

A Professional Association

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James A. Griner, CPA
Lori J. Carmichael, CPA
Daniel C. Moulton, CPA
Jack D. Kenney, CPA

INDEPENDENT AUDITOR'S REPORT

March 22, 2013

To the Supervisory Committee of
Farmers Insurance Group Federal Credit Union

We have audited the accompanying financial statements of Farmers Insurance Group Federal Credit Union, which comprise the statements of financial condition as of December 31, 2012 and 2011, and the related statements of income, comprehensive income, members' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

OCM&Co
A PROFESSIONAL ASSOCIATION
CPAs

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Farmers Insurance Group Federal Credit Union as of December 31, 2012 and 2011, 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.

Orth, Chakler, Murnane & Co.

Orth, Chakler, Murnane & Company
Certified Public Accountants
Miami, FL

OCM&Co
A PROFESSIONAL ASSOCIATION
CPAS

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION
STATEMENTS OF FINANCIAL CONDITION

ASSETS

	As of December 31, 2012	2011
Cash	$2,261,269	$2,022,738
Investments:		
Available-for-sale	24,981,490	30,613,127
Held-to-maturity	27,529,465	11,692,000
Other	55,766,973	50,366,217
Loans to members, net of allowance for loan losses	481,127,580	472,678,960
Accrued interest receivable:		
Investments	69,065	31,930
Loans	2,344,591	2,446,012
Other real estate owned (OREO)	2,438,510	1,151,741
Prepaid and other assets	6,854,099	4,837,482
Property and equipment, net	1,744,630	1,900,285
NCUSIF deposit	5,154,807	5,042,604
Total assets	$610,272,479	$582,783,096

LIABILITIES AND MEMBERS' EQUITY

	As of December 31, 2012	2011
LIABILITIES:		
Members' shares and deposits	$527,632,525	$503,717,346
Interest payable	303,636	333,828
Accounts payable and accrued liabilities	5,019,216	6,104,143
Total liabilities	532,955,377	510,155,317
Commitments and contingent liabilities		
MEMBERS' EQUITY:		
Regular reserve	16,966,743	16,966,743
Undivided earnings	60,151,751	55,533,838
Accumulated other comprehensive income	198,608	127,198
Total members' equity	77,317,102	72,627,779
Total liabilities and members' equity	$610,272,479	$582,783,096

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

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION
STATEMENTS OF INCOME

	For the years ended December 31, 2012	2011
INTEREST INCOME:		
Loans to members	$28,396,964	$29,054,906
Investments	540,866	843,015
Total interest income	28,937,830	29,897,921
INTEREST EXPENSE:		
Members' shares and deposits	3,875,065	4,345,794
Net interest income	25,062,765	25,552,127
PROVISION FOR LOAN LOSSES	1,303,370	121,148
Net interest income after provision for loan losses	23,759,395	25,430,979
NON-INTEREST INCOME:		
Overdraft and checking fees	3,365,859	3,363,648
Service charges and other fees	2,444,601	2,351,470
Interchange income	1,233,872	1,211,432
Other	680,704	693,538
Total non-interest income	7,725,036	7,620,088
	31,484,431	33,051,067
NON-INTEREST EXPENSE:		
Compensation and employee benefits	12,572,741	12,586,200
Office operating costs	5,937,955	5,178,675
Educational and promotional expense	1,933,067	746,491
Loan servicing expense	1,646,783	1,770,015
Office occupancy	1,345,533	1,329,558
Other expenses	1,268,365	884,586
Loss on sale of OREO, net	1,046,166	230,785
Professional and outside services	626,201	640,796
Corporate credit union stabilization fund assessments	489,707	1,260,651
Total non-interest expense	26,866,518	24,627,757
Net income	$4,617,913	$8,423,310

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

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION
STATEMENTS OF COMPREHENSIVE INCOME

	For the years ended December 31, 2012	2011
NET INCOME	$4,617,913	$8,423,310
OTHER ITEMS OF COMPREHENSIVE INCOME:		
Net unrealized gain on investments classified as available-for-sale	71,410	50,791
Other comprehensive income	71,410	50,791
Comprehensive income	$4,689,323	$8,474,101

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

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION
STATEMENTS OF MEMBERS' EQUITY

	For the years ended December 31, 2012 and 2011			
	Regular Reserve	Undivided Earnings	Accumulated Other Comprehensive Income	Total
Balance, December 31, 2010	$16,966,743	$47,110,528	$76,407	$64,153,678
Net income	—	8,423,310	—	8,423,310
Other comprehensive income	—	—	50,791	50,791
Balance, December 31, 2011	16,966,743	55,533,838	127,198	72,627,779
Net income	—	4,617,913	—	4,617,913
Other comprehensive income	—	—	71,410	71,410
Balance, December 31, 2012	$16,966,743	$60,151,751	$198,608	$77,317,102

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

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION
STATEMENTS OF CASH FLOWS

	For the years ended December 31, 2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$4,617,913	$8,423,310
Adjustments:		
Provision for loan losses	1,303,370	121,148
Depreciation and amortization	911,721	974,625
Amortization of investment premiums/discounts, net	15,044	—
Loss on sale of OREO, net	1,046,166	230,785
Changes in operating assets and liabilities:		
Accrued interest receivable	64,286	(3,411)
Prepaid and other assets	(2,016,617)	(798,995)
Interest payable	(30,192)	(62,385)
Accounts payable and accrued liabilities	(1,084,927)	1,972,033
Net cash provided by operating activities	4,826,764	10,857,110
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from maturities and repayments of available-for-sale investments	5,703,047	4,994,946
Proceeds from maturities and repayments of held-to-maturity investments	10,348,000	12,122,000
Purchase of available-for-sale investments	—	(32,000,000)
Purchase of held-to-maturity investments	(26,200,509)	(1,344,000)
Net change in other investments	(5,400,756)	20,630,060
Net change in loans, net of charge-offs	(14,162,654)	(6,317,818)
Recoveries on loans charged off	617,809	435,899
Proceeds from sale of OREO	1,459,920	889,907
Expenditures for property and equipment	(756,066)	(568,296)
Change in NCUSIF deposit	(112,203)	258,764
Net cash used in investing activities	(28,503,412)	(898,538)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net change in members' shares and deposits	23,915,179	(9,818,297)
Net cash provided by/(used in) financing activities	23,915,179	(9,818,297)
Net change in cash	238,531	140,275
Cash at beginning of year	2,022,738	1,882,463
Cash at end of year	$2,261,269	$2,022,738

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

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION
STATEMENTS OF CASH FLOWS

Cash Flows: (continued)

	For the years ended December 31,	
	2012	**2011**
SUPPLEMENTAL CASH FLOW DISCLOSURES:		
Interest paid	$3,905,257	$4,408,179
SCHEDULE OF NON-CASH TRANSACTIONS:		
Other comprehensive income	$71,410	$50,791
Transfer from loans to members to OREO	$3,792,855	$971,335

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

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION
NOTES TO THE FINANCIAL STATEMENTS

NOTE 1: SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION

Farmers Insurance Group Federal Credit Union (the Credit Union), is a cooperative association organized in accordance with the provisions of the Federal Credit Union Act for the purpose of promoting thrift among, and creating a source of credit for, its members. Participation in the Credit Union is limited to those who qualify for membership. The field of membership is defined by the Credit Union's Charter and Bylaws.

FINANCIAL STATEMENTS/USE OF ESTIMATES

The preparation of financial statements in accordance 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 the disclosure of contingent assets and liabilities as of the dates of the financial statements and the reported amounts of revenues and expenses for the periods then ended. Estimates that are particularly susceptible to change relate to the determination of the allowance for loan losses and the fair value of financial instruments. The significant accounting principles and policies used in the preparation of these financial statements, together with certain related information, are summarized below.

CASH

Cash and cash equivalents includes amounts due from banks, credit unions and cash on hand. Amounts due from banks and credit unions may, at times, exceed federally insured limits.

INVESTMENTS

Investments are classified into the following categories: available-for-sale, held-to-maturity and other. Investment securities classified as available-for-sale are measured at fair value as of the statement of financial condition date. Unrealized gains and losses on available-for-sale investments are reported as a separate component of members' equity. Investment securities classified as held-to-maturity are measured at amortized cost. This classification is based upon the Credit Union's intent and ability to hold these investment securities to full maturity. Realized gains and losses on disposition, if any, are computed using the specific identification method. Investments are adjusted for the amortization of premiums and accretion of discounts as an adjustment to interest income on investments over the term of the investment by a method which approximates the interest method. The Credit Union has elected to classify certain cash equivalents as other investments. This election is available to the Credit Union according to the terms of the Statement of Cash Flows Topic of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC).

Note 1: (continued)

LOANS TO MEMBERS AND ALLOWANCE FOR LOAN LOSSES

Loans to members are stated at the amount of unpaid principal net of deferred loan origination fees and costs and an allowance for loan losses (ALL). The ALL is increased by a provision for loan losses charged to expense and decreased by charge-offs (net of recoveries). The ALL is maintained at a level considered adequate to provide for optimal loss coverage for the entire loan portfolio over the next twelve months. Individually significant, non-homogeneous loans are measured for impairment in accordance with the Subsequent Measurement of Receivables Topic of the FASB ASC. These loans are evaluated individually based on an examination of the current financial information of the borrower and an estimate of the value of the collateral, if any. If the carrying value of any of these loans is greater than the estimated net realizable value of the property or of the collateral securing these loans, a reserve is established for the difference. Management's periodic evaluation of the adequacy of the ALL also considers such factors as changes in the nature and volume of the loan portfolio, review of specific problem loans, and current economic conditions that may affect the borrower's ability to repay.

Interest on loans to members is recognized over the terms of the loans and is calculated on principal amounts outstanding. The accrual of interest is discontinued when a loan exceeds 90 days delinquent or when management believes that collection of interest is doubtful. Loan fees and direct loan origination costs are deferred and the net fee or cost is recognized as an adjustment to interest income on loans using a method that approximates the interest method over the estimated life of the loans.

ALL METHODOLOGY

Management has an established methodology to determine the adequacy of the ALL that assesses the risks and losses inherent in the entire loan portfolio. For the purpose of determining the ALL disclosures, the Credit Union has segmented loans in the portfolio by product type. Loans are divided into the following segments: Consumer, Residential Real Estate, and Commercial. The Credit Union further disaggregates these segments into classes based on the associated risks within those segments.

Consumer loans are divided into four classes: Other secured, Unsecured, New auto, and Used auto. Residential real estate loans are divided into three classes: First mortgage, Second mortgage, and Home equity line of credit (HELOC). Commercial loans are all classified as real estate. Each class of loans requires significant judgment to determine the estimation method that fits the credit risk characteristics of its portfolio segment. The Credit Union uses both internally developed and vendor supplied models in the process. The vendor model is supplied by Portfolio 360, Inc. The Portfolio 360, Inc. model provides meaningful insights into the portfolio's risk composition, as dictated by the intrinsic value and other relevant market data. The model is specifically designed to calculate the risk of the loan portfolio on an individual loan level basis to provide optimal loss coverage analysis over the next 12 months.

Note 1: (continued)

Management must use judgment in establishing additional input metrics for the modeling processes. The models and assumptions used to determine the ALL 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 is how management determines the balance of the ALL for each segment or class of loans.

CONSUMER PORTFOLIO SEGMENT ALL METHODOLOGY

For consumer loans, the Credit Union determines the ALL on a collective basis utilizing historical and forecasted losses to represent the best estimate of inherent losses at the measurement date. Loans are pooled, generally by loan types with similar risk characteristics. The Credit Union identifies consumer loans that underwent a troubled debt restructuring and evaluates these loans on an individual basis. In addition, the ALL model incorporates numerous other historical factors based upon the borrower, collateral type, loan performance, environment, and economy. These historical factors used in the analysis date back to 2001.

As appropriate, to achieve greater accuracy, further stratification of a selected portfolio may occur such as by year of origination, geographic location and other predictive characteristics. The consumer ALL model primarily uses historical delinquency and default experience. Information on forecasted delinquency analysis, member credit score trends, unemployment trends, industry trends and other key economic variables that may influence the frequency and severity of losses for each class of loan within the consumer segment may also be considered.

The Credit Union's consumer loan portfolio also includes loans collateralized by contract value. These are considered fully secured unless notified otherwise, as these loans, when written within the guidelines established by Farmers Insurance Group Inc. (Farmers), are secured and will be paid in full by Farmers upon member termination if the Credit Union's collection efforts were to ultimately fail. Similarly, loans collateralized by a certificate or share account are also considered fully secured unless otherwise notified.

RESIDENTIAL REAL ESTATE PORTFOLIO SEGMENT ALL METHODOLOGY

For residential real estate loans not identified as impaired, the Credit Union determines the ALL on a collective basis, utilizing various economic and financial simulations in order to determine the best estimate of inherent losses at the measurement date. Loans are pooled, generally by loan types with similar risk characteristics. In addition, the ALL model incorporates numerous other historical factors based upon the borrower, collateral type, loan performance, environment, and economy. These historical factors used in the analysis date back to 2001.

As appropriate, to achieve greater accuracy, further stratification of a selected portfolio may occur such as by year of origination, geographic location and other predictive characteristics. Information on member credit score trends, combined loan to value ratios, home price trends, unemployment trends, industry trends, and other key economic variables that may influence the frequency and severity of losses for each class of loan within the residential real estate segment may also be considered. The residential real estate ALL also includes an amount for the estimated losses on individually evaluated impaired loans.

Note 1: (continued)

Additionally, a mortgage sample analysis is performed periodically to assess the potential loss exposure within the residential real estate loan portfolio. The Credit Union obtains updated property values on all existing real estate loans in its portfolio. Using a sample of loans, the Credit Union performs individual reviews to assess the potential loss exposure based on various risk factors including combined loan to value, member credit score, delinquency, loan vintage, and type of collateral. Results of the sample analysis are extrapolated to the total population to assess the adequacy of the ALL.

COMMERCIAL PORTFOLIO SEGMENT ALL METHODOLOGY

For commercial loans not identified as impaired, the Credit Union determines the ALL on a collective basis utilizing historical and forecasted losses to represent the best estimate of inherent losses at the measurement date. In addition, the ALL model incorporates numerous other historical factors based upon the borrower, collateral type, loan performance, environment, and economy. These historical factors used in the analysis date back to 2001.

Loss estimates for the commercial loan portfolio segment may be adjusted as appropriate based on credit risk assessment and management's analysis of leading predictors of losses, as well as additional analysis of long-term average loss experience compared to previously forecasted losses, external loss data, or other risks identified from current economic conditions and credit quality trends. The commercial ALL may also include an additional ALL for individually evaluated high risk loans and an amount for the estimated losses on individually evaluated impaired loans.

LOAN CHARGE-OFF POLICIES

The Credit Union’s quality control process includes preparing lists to monitor and track delinquent and special mention loans. Tracking loans on these lists enables management to assess the performance of the loan portfolio and act to mitigate risk therein through necessary changes in policy and procedures. The quality control process also serves as a tool to assist the Credit Union in identifying loans for charge-off on a timely basis. The following is a description of the Credit Union’s loan charge-off policies:

Consumer, residential real estate, and commercial loans are generally charged-off when the loan is deemed to be uncollectible. A loan is deemed uncollectible when:

- the member has gained relief through bankruptcy;
- the loan is a deficiency balance from the sale of collateral and the borrower has indicated an unwillingness to make further payments;
- the borrower is determined to be a “skip”;
- the member is deceased, collateral has been liquidated and there is no co-maker or estate to pursue for payment;
- the loan is 180 days or more delinquent, unless one of the following conditions exists:

Note 1: (continued)

- the borrower is making monthly payments but cannot qualify for refinancing or re-aging;
- the Credit Union or the member is waiting for settlement of a documented insurance/bond claim;
- the borrower is deceased, and the Credit Union has substantial reason to expect settlement from the estate, co-makers, or relatives;
- the Credit Union is waiting for the proceeds from the sale of repossessed collateral.

Uncollectible loans to be charged off to the ALL are approved by the Board of Directors each month. For repossessed collateral, including foreclosed property, the loan is charged off to the ALL and the net realizable value moved to other assets.

OTHER REAL ESTATE OWNED (OREO)
Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell.

PROPERTY AND EQUIPMENT
Property and equipment are carried at cost less accumulated depreciation. 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 term of the lease, or the estimated life of the asset, whichever is less. The Credit Union reviews property and equipment (long-lived assets) for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

NCUSIF DEPOSIT
The deposit in the National Credit Union Share Insurance Fund (NCUSIF) is in accordance with National Credit Union Administration (NCUA) regulations, which require the maintenance of a deposit by each federally insured credit union in an amount equal to 1% of its insured members' 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.

CORPORATE CREDIT UNION STABILIZATION FUND ASSESSMENTS
During September 2011 and July 2012, the NCUA Board approved 25 and 9.5 basis point assessments to fund the corporate credit union stabilization fund. These assessments were based on the Credit Union's insured shares as of June 30, 2011 and 2012, respectively. **(See Note 11)**

Note 1: (continued)

MEMBERS' SHARES AND DEPOSITS

Members' shares are subordinated to all other liabilities of the Credit Union upon liquidation. Interest on members' shares and deposits is based on available earnings at the end of an interest period and is not guaranteed by the Credit Union. Interest rates on members' share accounts are set by the Board of Directors, based on an evaluation of current and future market conditions.

REGULAR RESERVE

The Credit Union is required to maintain a statutory reserve (regular reserve) in accordance with the Federal Credit Union Act. This statutory reserve represents a regulatory restriction and is not available for the payment of interest.

FEDERAL AND STATE TAX EXEMPTION

The Credit Union is exempt from most federal, state, and local taxes under the provisions of the Internal Revenue Code and state tax laws. The Income Taxes Topic of the FASB ASC clarifies accounting for uncertainty in income taxes reported in the financial statements. The interpretation provides criteria for assessment of individual tax positions and a process for recognition and measurement of uncertain tax positions. Tax positions are evaluated on whether they meet the "more likely than not" standard for sustainability on examination by tax authorities. Federal credit unions are tax-exempt under Internal Revenue Code sections 501(c)(1)(a)(I) and 501(c)(14)(A). As such, the Credit Union has no uncertain tax positions that qualify for either recognition or disclosure in the financial statements. Additionally, no interest or penalties have been recorded in the accompanying financial statements related to uncertain tax positions.

RECLASSIFICATIONS

Certain 2011 financial statement amounts have been reclassified to conform with classifications adopted in 2012.

SUBSEQUENT EVENTS

Management has evaluated subsequent events through March 22, 2013, the date the financial statements were available to be issued. Management has not identified any items requiring recognition or disclosure.

NOTE 2: INVESTMENTS

The amortized cost and estimated fair value of investments are as follows:

	As of December 31, 2012			
Available-for-sale:	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
Mortgage-backed securities	$2,705,649	$93,229	$—	$2,798,878
NCUA guaranteed notes	22,015,387	104,808	—	22,120,195
Collateralized-mortgage obligations	61,846	571	—	62,417
	$24,782,882	$198,608	$—	$24,981,490

	As of December 31, 2011			
Available-for-sale:	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
Mortgage-backed securities	$3,032,660	$100,765	$—	$3,133,425
NCUA guaranteed notes	27,397,329	26,477	—	27,423,806
Collateralized-mortgage obligations	55,940	—	(44)	55,896
	$30,485,929	$127,242	($44)	$30,613,127

All available-for-sale investments receive principal and interest payments based on the payments received on the loans underlying the investments. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay certain obligations without call or prepayment penalties.

	As of December 31, 2012			
Held-to-maturity:	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
Brokered certificates of deposit	$27,529,465	$—	$—	$27,529,465

	As of December 31, 2011			
Held-to-maturity:	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
Brokered certificates of deposit	$11,692,000	$—	$—	$11,692,000

Note 2: (continued)

The amortized cost and estimated fair value of held-to-maturity investments by contractual maturity are shown below.

	As of December 31, 2012 *Held-to-maturity*	
	Amortized Cost	**Fair Value**
Within 1 year	$8,918,304	$8,918,304
1 to 5 years	18,611,161	18,611,161
	$27,529,465	$27,529,465

Other investments:	**As of December 31,**	
	2012	**2011**
Federal Reserve Bank	$41,571,883	$—
Corporate credit union deposits	10,195,090	50,366,217
CUSO investment	4,000,000	—
	$55,766,973	$50,366,217

The Credit Union maintains deposits at corporate credit unions which normally exceed federally insured limits; however, NCUA is providing a temporary guarantee on deposits in excess of insurance limits maintained at corporate credit unions through December 31, 2012, other than perpetual contributed capital, membership capital shares and paid-in capital. These uninsured deposits are subject to certain withdrawal restrictions and approximated $600,000 and $4,101,000 as of December 31, 2012 and 2011, respectively.

The following table shows the gross unrealized losses and fair value of investments, aggregated by length of time individual securities have been in a continuous unrealized loss position.

	As of December 31, 2011 *Available-for-sale*					
	Less than 12 Months		***12 Months or Longer***		***Total***	
	Fair Value	**Gross Unrealized Losses**	**Fair Value**	**Gross Unrealized Losses**	**Fair Value**	**Gross Unrealized Losses**
Collateralized-mortgage obligations	$55,896	$44	$—	$—	$55,896	$44

Unrealized losses on securities issued by the U.S. Government and its Agencies have not been recognized into income because the principal balances of these securities are guaranteed by the U.S. Government. Additionally, management has the ability and intent to hold these securities through to recovery of fair value, which may be maturity.

NOTE 3: LOANS TO MEMBERS

The composition of loans to members is as follows:

	As of December 31, 2012	2011
Consumer:		
Other secured	$176,875,627	$175,433,506
Unsecured	70,548,971	60,552,682
New auto	22,429,999	17,206,939
Used auto	41,424,975	35,976,764
Total consumer	311,279,572	289,169,891
Residential Real Estate:		
First mortgage	81,526,726	87,307,850
Second mortgage	11,336,161	15,060,166
HELOC	10,581,058	12,016,990
Total residential real estate	103,443,945	114,385,006
Commercial:		
Real estate	77,711,864	81,899,429
Total loans	492,435,381	485,454,326
Deferred loan origination fees/costs, net	(615,943)	203,565
	491,819,438	485,657,891
Less ALL	(10,691,858)	(12,978,931)
	$481,127,580	$472,678,960

A summary of the activity in the ALL by portfolio segment is as follows:

	For the years ended December 31, 2012 and 2011			
	Consumer	Residential Real Estate	Commercial	Total
Balance, December 31, 2010	$3,214,824	$5,883,304	$7,719,805	$16,817,933
Provision for loan losses	1,730,980	(557,831)	(1,052,001)	121,148
Recoveries	215,036	153,246	67,617	435,899
Loans charged off	(2,205,962)	(909,934)	(1,280,153)	(4,396,049)
Balance, December 31, 2011	2,954,878	4,568,785	5,455,268	12,978,931
Provision for loan losses	734,585	(522,840)	1,091,625	1,303,370
Recoveries	282,429	251,446	83,934	617,809
Loans charged off	(1,842,668)	(922,616)	(1,442,968)	(4,208,252)
Balance, December 31, 2012	$2,129,224	$3,374,775	$5,187,859	$10,691,858

Note 3: (continued)

	As of December 31, 2012			
	Consumer	Residential Real Estate	Commercial	Total
Individually evaluated for impairment	$93,067	$2,219,078	$4,722,735	$7,034,880
Collectively evaluated for impairment	$2,036,157	$1,155,697	$465,124	$3,656,978

	As of December 31, 2011			
	Consumer	Residential Real Estate	Commercial	Total
Individually evaluated for impairment	$118,294	$2,014,701	$4,763,814	$6,896,809
Collectively evaluated for impairment	$2,836,584	$2,554,084	$691,454	$6,082,122

A summary of the recorded investment in loans, by portfolio segment, is as follows:

	As of December 31, 2012			
	Consumer	Residential Real Estate	Commercial	Total
Ending balance	$311,279,572	$103,205,505	$77,334,361	$491,819,438
Individually evaluated for impairment	$456,046	$8,726,451	$16,758,224	$25,940,721
Collectively evaluated for impairment	$310,823,526	$94,479,054	$60,576,137	$465,878,717

	As of December 31, 2011			
	Consumer	Residential Real Estate	Commercial	Total
Ending balance	$289,169,891	$114,575,258	$81,912,742	$485,657,891
Individually evaluated for impairment	$776,698	$9,964,704	$22,171,910	$32,913,312
Collectively evaluated for impairment	$288,393,193	$104,610,554	$59,740,832	$452,744,579

IMPAIRED LOANS

A loan is impaired when it is probable, based on current information and events, that the Credit Union will be unable to collect all contractual principal and interest payments due in accordance with the terms of the loan agreement. When management identifies a loan as impaired, the impairment is measured 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 management uses the current fair value of the collateral, less selling costs when foreclosure is probable, instead of discounted cash flows. If management determines that the value of the impaired loan is less than the recorded investment in the loan, impairment is recognized through an ALL estimate or a charge-off to the ALL.

Note 3: (continued)

The following tables include the recorded investment and unpaid principal balances for impaired loans with the associated ALL amount, if applicable. Also presented are the average recorded investments in the loans and the related amount of interest recognized during the time within the period that the loans were individually evaluated for impairment. Interest is credited to interest income when received, under the cash basis method. The average balances are calculated based on the year-end balances of the loans of the period reported.

Payments received on impaired loans are recorded as a reduction of principal or as interest income depending on management's assessment of the ultimate collectability of the loan principal. Generally, interest income on an impaired loan is recorded on a cash basis when the outstanding principal is brought current. Interest income recorded on impaired loans for all periods presented was recorded on a cash basis.

The tables below summarize key information for impaired loans:

	As of December 31, 2012			**For the year ended December 31, 2012**	
	Recorded Investment	Unpaid Principal Balance	Specific Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance:					
Consumer:					
Other secured	$—	$—	$—	$23,038	$2,598
With an allowance recorded:					
Consumer:					
Other secured	$177,176	$177,176	$33,314	$180,991	$9,588
Unsecured	$206,382	$206,382	$38,579	$227,251	$20,252
New auto	$9,646	$9,646	$545	$21,253	$9
Used auto	$62,842	$62,842	$20,629	$163,839	$3,113
Residential Real Estate					
First mortgage	$8,527,792	$8,552,805	$1,959,261	$9,155,145	$398,811
Second mortgage	$178,573	$178,573	$95,662	$180,390	$12,428
HELOC	$20,086	$19,596	$164,155	$10,043	$784
Commercial:					
Real estate	$16,758,224	$17,159,002	$4,722,735	$19,465,067	$968,484
Totals:					
Consumer	$456,046	$456,046	$93,067	$616,372	$35,560
Residential Real Estate	$8,726,451	$8,750,974	$2,219,078	$9,345,578	$412,023
Commercial	$16,758,224	$17,159,002	$4,722,735	$19,465,067	$968,484

Note 3: (continued)

	As of December 31, 2011			For the year ended December 31, 2011	
	Recorded Investment	Unpaid Principal Balance	Specific Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance:					
Consumer:					
Other secured	$46,075	$46,075	$—	$23,038	$2,598
With an allowance recorded:					
Consumer:					
Other secured	$184,806	$184,806	$46,144	$152,031	$10,422
Unsecured	$248,120	$248,119	$46,968	$156,924	$27,243
New auto	$32,861	$32,861	$2,781	$29,462	$1,510
Used auto	$264,836	$264,836	$22,401	$247,249	$14,278
Residential Real Estate					
First mortgage	$9,782,497	$9,766,281	$1,964,235	$9,371,570	$508,863
Second mortgage	$182,207	$181,905	$50,466	$217,479	$12,615
Commercial:					
Real estate	$22,171,910	$22,168,307	$4,763,814	$20,987,292	$1,325,576
Totals:					
Consumer	$776,698	$776,697	$118,294	$608,704	$56,051
Residential Real Estate	$9,964,704	$9,948,186	$2,014,701	$9,589,049	$521,478
Commercial	$22,171,910	$22,168,307	$4,763,814	$20,987,292	$1,325,576

The tables below provide an age analysis of past due loans by class:

	As of December 31, 2012					
	Days Delinquent			Total Delinquent Loans	Total Current Loans	Total Loans
	30 - 59	60 - 89	90 or more			
Consumer:						
Other secured	$88,168	$24,979	$169,295	$282,442	$176,593,185	$176,875,627
Unsecured	731,768	330,503	219,416	1,281,687	69,267,284	70,548,971
New auto	43,634	—	18,126	61,760	22,368,239	22,429,999
Used auto	158,844	124,816	126,285	409,945	41,015,030	41,424,975
Residential Real Estate:						
First mortgage	977,545	—	1,235,591	2,213,136	79,075,150	81,288,286
Second mortgage	146,432	230,104	—	376,536	10,959,625	11,336,161
HELOC	250,345	—	43,572	293,917	10,287,141	10,581,058
Commercial:						
Real estate	634	—	3,733,144	3,733,778	73,600,583	77,334,361
Total	$2,397,370	$710,402	$5,545,429	$8,653,201	$483,166,237	$491,819,438

Note 3: (continued)

As of December 31, 2011

	Days Delinquent			Total Delinquent Loans	Total Current Loans	Total Loans
	30 - 59	60 - 89	90 or more			
Consumer:						
Other secured	$794	$—	$574	$1,368	$175,432,138	$175,433,506
Unsecured	742,638	257,533	265,965	1,266,136	59,286,546	60,552,682
New auto	118,481	35,754	37,854	192,089	17,014,850	17,206,939
Used auto	221,876	182,705	126,915	531,496	35,445,268	35,976,764
Residential Real Estate:						
First mortgage	425,624	2,095	3,112,626	3,540,345	83,628,502	87,168,847
Second mortgage	26,915	102,383	7,779	137,077	14,923,089	15,060,166
HELOC	165,099	—	—	165,099	12,181,146	12,346,245
Commercial:						
Real estate	221,241	—	8,529,377	8,750,618	73,162,124	81,912,742
Total	$1,922,668	$580,470	$12,081,090	$14,584,228	$471,073,663	$485,657,891

The Credit Union places loans on non-accrual status when the loan reaches 90 days past due or when the collection of interest or principal becomes uncertain. Loans on which the accrual of interest has been discontinued or reduced approximated $5,569,000 and $12,081,000 as of December 31, 2012 and 2011, respectively. There were no loans 90 days or more past due and still accruing interest as of December 31, 2012 or 2011.

TROUBLED DEBT RESTRUCTURING

The Credit Union's loan portfolio also includes certain loans that have been modified in a Troubled Debt Restructuring (TDR), 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.

When the Credit Union modifies a collateral dependent loan, management uses the current fair value of the collateral, less selling costs, to determine the net realizable value of the collateral. If management determines that the value of the modified loan is less than the recorded investment in the loan, impairment is recognized by segment or class of loan, as applicable, through the ALL.

The following tables include TDRs approved during the period. There were no TDRs performed during the periods that then defaulted in the same period. The Credit Union defines a TDR as subsequently defaulted when the TDR is 90 days past due or the member files bankruptcy.

Note 3: (continued)

The following table presents the TDRs performed by class of loans during the year ended December 31, 2012:

	Number	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Residential Real Estate:			
First mortgage	2	$710,437	$703,334
Commercial:			
Real estate	4	947,133	1,178,272
		$1,657,570	$1,881,606

The following table presents the TDRs performed by class of loans during the year ended December 31, 2011:

	Number	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Residential Real Estate:			
First mortgage	1	$329,177	$326,678
Commercial:			
Real estate	5	4,298,798	4,291,904
		$4,627,975	$4,618,582

CREDIT QUALITY INDICATORS

The Credit Union uses the Portfolio 360, Inc. model to monitor credit quality for the consumer, residential real estate, and commercial loan portfolios. The Portfolio 360, Inc. model analyzes each loan's risk. When analyzing each loan, the model identifies a set of numbers, or vectors, which represent the borrower's probability of default and the loss severity of the loan over a set of different economic scenarios. These vectors are used to calculate the loan risk grade and run risk adjusted cash flows which result in the value-at-risk, pricing, and loan valuation.

The model incorporates over 150 data points covering more than just credit score and collateral value. These loan level factors include institution and borrower specific data points as well as economic measures that feed into the risk analysis. They provide value reconciliation when refreshing property values and add updated values for the new and used auto portfolios. They continue to enhance the risk model by incorporating new technologies and applying all loan data available.

Note 3: (continued)

In addition to credit score, the model incorporates numerous other factors based upon the borrower, collateral, loan performance, environment, institution, and economy as follows:

Macro-economic - This segment's data points are used to depict the overall health of the national economy such as: national unemployment, GDP growth, Treasury rate curves and forecasts, industry delinquencies and charge-offs, national credit scores, borrower bankruptcy rates, etc.

Institution - This segment focuses on the Credit Union and is used to model the borrower's profile, stability, and fine tune the risk adjustments to the specific institution. Examples of data points include delinquency rates and trends, charge-offs, and bankruptcies per 1,000 members.

Regional geography - This segment focuses on local economic factors such as unemployment, growth, and real estate values.

Loan - Additional data points added to this analysis are payment trend, auto pay, updated senior balances, last payment amounts, and use of proceeds.

Borrower - Examples of data points in this segment are disposable income, updated cash reserves, employment status, and direct deposit.

Asset - In addition to using different automated valuation model products for the residential portfolio, the model includes new data to improve vehicle valuations for the new and used auto portfolios.

The following tables represent the recorded investment of consumer, residential real estate, and commercial loan credit exposures by Portfolio 360, Inc. risk grade as of December 31, 2012 and 2011. The use of the Portfolio 360, Inc. risk grades permits management to estimate a portion of credit risk. Category ratings are reviewed quarterly, at which time management analyzes the resulting grades, as well as other external statistics and factors, to track loan performance. Loans that trend upward toward higher levels generally have a higher risk factor associated. Whereas, loans that migrate toward lower ratings generally will result in a lower risk factor being applied to those related loan balances. The risk ratings from Business Partners are taken into consideration when the Penrith risk grades are applied to the individual commercial real estate loan participations.

The Penrith risk grades are as follows:

V1 - Minimal risk - These loans generally show the ability to cover expenses with a minimal chance of default. The typical characteristics for these loans are long-term Credit Union members with excellent credit history, strong cash flow, quality money management, excellent access to alternative sources of financing, and well collateralized. These loans typically have very low potential loss, no greater than one percent of the loan balance in most cases when factoring the default probability and loss severity.

Note 3: (continued)

V2 - Low risk - These loans generally reflect good payment history, a healthy loan to value ratio and are adequately collateralized. The borrowing entity has very good to excellent credit, steady cash flow, quality money management, and good access to alternative sources of financing. As a result, the risk category is highly unlikely to experience a loss. If a loss does occur, it is likely to be minimal.

V3 - Acceptable risk - These loans are better than average loans with a low chance of a loss. The potential loss should be no greater than five percent of the loan balance when factoring default probability and loss severity. Most of the risk attributes for these loans are in line with a low risk profile but are on the fringe of adding risk. Borrower has some access to alternative sources of financing, good money management, and shows control of expenses.

V4 - Moderate risk - These loans have potential weaknesses or may show a propensity to deteriorate further. These loans are the start of the tipping point of the mid-range risk grades (V4 - V6) that tend to move either to a worsening position or a healthier position and is measured by a ten percent value at risk. This risk grade may include borrowers with only medium to fair credit ratings and a few recent problems. Cash flow is steady and generally adequate to service debt but my be subject to cyclical conditions. The borrower may have limited access to alternative financing.

V5 - Special mention - These loans can prove to be in the most critical stage. Most loans tend to either move up or down from the mid-range risk grades (V4 - V6). Both credit and collateral are substandard, with external economic factors bearing down. The outstanding loan balance may not be entirely protected by equity in the underlying asset with up to a fifteen percent potential loss produced by probability and severity. There may be one or more specific weaknesses jeopardizing the loan, and the Credit Union will most likely sustain a loss if the deficiencies are not corrected.

V6 - Increased risk - These loans generally have multiple vulnerable and weak risk factors that could be attributed to local economic factors. On the basis of currently known facts, the combination of weak attributes make collection or liquidation in full highly questionable and improbable. The risk grade is defined by potential losses of up to twenty percent of the loan balance.

V7 - Elevated risk - There is a strong probability that the Credit Union may not be able to recover on these loans. The Credit Union and the member must look at all options, including modification. Liquidation needs to be considered because most of the underlying assets for this risk grade have passed the tipping point. A loss is nearly impossible to avoid on repayment, refinancing, or liquidation for these loans. The value at risk could be upwards of thirty percent of the current loan balance.

V8 - Doubtful - These borrowers are most likely in a loss situation and can be measured by potential value at risk between thirty and forty percent of the outstanding loan balance. In most cases, assets in this region do not recover and the members and properties are being worked with directly. The most current information on the member and asset has been acquired and the Credit Union has a firm estimate of the loss when the time arrives.

Note 3: (continued)

V9 - Inherent loss - These loans are considered uncollectible and will be charged off immediately. Assets in this risk area have an inherent value at risk, north of forty percent. Modification is impossible without major concessions or write down. Residential and commercial properties have a high probability of becoming other real estate owned. In some cases, the Credit Union may find a glimmer of success in short sale opportunities. Other real estate owned, having extended liquidation times and expenses are most likely in less than optimal locations. Conditions prove challenging to draw respectable tenants and rent.

The tables below summarize key information for consumer credit quality:

Consumer Credit Quality Indicators
As of December 31, 2012

Risk grade	Other Secured	Unsecured	New auto	Used auto	Total
V1	$—	$34,178,194	$20,567,561	$34,196,571	$88,942,326
V2	—	21,612,649	1,256,627	4,563,227	27,432,503
V3	—	6,504,213	357,926	1,663,873	8,526,012
V4	—	5,048,673	212,069	827,073	6,087,815
V5	—	1,076,450	34,810	107,253	1,218,513
V6	—	222,522	—	53,863	276,385
V7	—	429,233	—	11,247	440,480
V8	—	52,208	—	—	52,208
V9	—	357,945	—	—	357,945
No risk grade	176,875,627	1,066,884	1,006	1,868	177,945,385
	$176,875,627	$70,548,971	$22,429,999	$41,424,975	$311,279,572

Consumer Credit Quality Indicators
As of December 31, 2011

Risk grade	Other Secured	Unsecured	New auto	Used auto	Total
V1	$—	$57,602	$15,119,237	$24,323,434	$39,500,273
V2	—	16,095,261	1,325,565	6,047,219	23,468,045
V3	—	30,055,108	593,705	3,897,842	34,546,655
V4	—	9,168,514	122,161	1,269,824	10,560,499
V5	—	1,501,885	—	180,892	1,682,777
V6	—	2,450,519	—	19,123	2,469,642
V7	—	291,275	—	34,363	325,638
V8	—	147,172	—	—	147,172
V9	—	404,402	—	—	404,402
No risk grade	175,433,506	380,944	46,271	204,067	176,064,788
	$175,433,506	$60,552,682	$17,206,939	$35,976,764	$289,169,891

Note 3: (continued)

The tables below summarize key information for residential real estate credit quality:

Residential Real Estate Credit Quality Indicators
As of December 31, 2012

Risk grade	First mortgage	Second mortgage	HELOC	Total
V1	$48,870,135	$3,119,681	$5,917,457	$57,907,273
V2	8,582,084	998,924	803,017	10,384,025
V3	5,477,513	1,619,428	462,446	7,559,387
V4	6,748,348	1,982,656	986,395	9,717,399
V5	4,426,166	985,817	403,117	5,815,100
V6	2,035,304	794,624	32,821	2,862,749
V7	2,602,445	1,160,070	460,999	4,223,514
V8	612,147	284,862	117,510	1,014,519
V9	1,743,374	390,099	98,977	2,232,450
No risk grade	190,770	—	1,298,319	1,489,089
	$81,288,286	$11,336,161	$10,581,058	$103,205,505

Residential Real Estate Credit Quality Indicators
As of December 31, 2011

Risk grade	First mortgage	Second mortgage	HELOC	Total
V1	$51,923,620	$5,635,606	$6,790,242	$64,349,468
V2	6,569,168	1,073,529	1,138,712	8,781,409
V3	6,843,653	1,504,737	571,019	8,919,409
V4	4,552,706	1,305,514	793,441	6,651,661
V5	7,113,387	3,205,027	2,189,948	12,508,362
V6	4,744,639	1,412,877	523,596	6,681,112
V7	1,298,908	587,735	47,848	1,934,491
V8	2,057,414	177,472	—	2,234,886
V9	287,718	157,669	291,439	736,826
No risk grade	1,777,634	—	—	1,777,634
	$87,168,847	$15,060,166	$12,346,245	$114,575,258

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION
NOTES TO THE FINANCIAL STATEMENTS

Note 3: (continued)

The tables below summarize key information for commercial credit quality:

Commercial Credit Quality Indicators
As of December 31, 2012

Risk grade	Real estate
V1	$32,070,081
V2	15,542,230
V3	10,450,301
V4	5,130,957
V5	3,179,200
V6	1,939,553
V7	6,793,067
V8	1,080,657
V9	558,107
No risk grade	590,208
Total	$77,334,361

Commercial Credit Quality Indicators
As of December 31, 2011

Risk grade	Real estate
V1	$41,862,362
V2	12,185,219
V3	5,332,022
V4	1,754,160
V5	10,380,175
V6	649,888
V7	—
V8	1,069,076
V9	5,965,198
No risk grade	2,714,642
Total	$81,912,742

NOTE 4: PROPERTY AND EQUIPMENT

A summary of the Credit Union's property and equipment is as follows:

	As of December 31, 2012	As of December 31, 2011
Furniture and equipment	$9,492,920	$9,102,435
Leasehold improvements	2,058,037	1,965,064
	11,550,957	11,067,499
Less accumulated depreciation and amortization	(9,806,327)	(9,167,214)
	$1,744,630	$1,900,285

NOTE 5: MEMBERS' SHARES AND DEPOSITS

Members' shares and deposits are summarized as follows:

	As of December 31, 2012	2011
Share drafts	$75,440,005	$67,061,182
Regular shares	82,084,993	69,724,304
Money market accounts	196,136,060	185,594,889
IRA shares	31,797,580	32,945,916
Share and IRA certificates	142,173,887	148,391,055
	$527,632,525	$503,717,346

The aggregate balance of members' time deposit accounts in denominations of $100,000 or more was approximately $73,788,000 and $75,105,000 as of December 31, 2012 and 2011, respectively. Negative share and share draft accounts reclassified to loans to members were approximately $427,000 and $288,000 as of December 31, 2012 and 2011, respectively.

Scheduled maturities of share and IRA certificates are as follows:

	As of December 31, 2012
Within 1 year	$93,420,777
1 to 2 years	22,234,100
2 to 3 years	15,271,960
3 to 4 years	4,866,673
4 to 5 years	6,369,360
Over 5 years	11,017
	$142,173,887

SHARE INSURANCE

As of December 31, 2012, members' shares were insured by the NCUSIF to a maximum of $250,000 for each member. Individual Retirement Accounts are insured by the NCUSIF for an additional $250,000 of coverage. Additionally, non-interest bearing share accounts are fully insured by the NCUSIF until December 31, 2012.

NOTE 6: EMPLOYEE BENEFITS

CASH BALANCE PROGRAM AND 401(K) PENSION PLAN

On January 1, 2009, the Credit Union's defined benefit pension plan was modified and only vested employees who were age 40 and over, or who had 10 years of service as of December 31, 2008, were grandfathered into the existing pension plan. All remaining and new employees became participants of the Cash Balance Program. Farmers Insurance Group, Inc. (Farmers) makes annual contributions to the employees' cash balance account, which is based on a percentage of the employees' salaries. Also, the noncontributory deferred profit sharing plan was terminated and replaced with a 401(k) plan through Farmers, which allows employees to defer a portion of their salary into the 401(k) plan up to certain limits established by the Internal Revenue Service. The Credit Union makes discretionary matching contributions each year. Participants are always 100% vested in all their voluntary contributions. The Credit Union's matching contributions become fully vested at the completion of three years of service.

Retirement plan costs are accrued and funded on a current basis. Total retirement plan costs paid by the Credit Union to Farmers for the years ended December 31, 2012 and 2011 amounted to approximately $830,000 and $952,000, respectively.

NOTE 7: COMMITMENTS AND CONTINGENT LIABILITIES

LEASE COMMITMENTS

The Credit Union leases several branch locations. The minimum remaining noncancellable lease obligations approximate the following as of December 31, 2012:

Year ending December 31,	Amount
2013	$967,000
2014	925,000
2015	927,000
2016	882,000
2017	868,000
Thereafter	1,443,000
	$6,012,000

Rental expense under operating leases was approximately $1,262,000 and $1,242,000 for the years ended December 31, 2012 and 2011, respectively.

LINES OF CREDIT

As of December 31, 2012, the Credit Union maintained two unused lines of credit with Catalyst Corporate Federal Credit Union, and one unused line of credit with Corporate America Credit Union. The terms of these agreements require the pledging of all presently owned and later acquired unencumbered assets as security for obligations under these line-of-credit agreements. As of December 31, 2012, the unused line of credit under the Catalyst Corporate Federal Credit Union agreement approximated $50,000,000, and the unused line of credit under the Corporate America Credit Union agreement approximated $30,000,000.

Note 7: (continued)

MISCELLANEOUS LITIGATION

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

NOTE 8: OFF-BALANCE-SHEET RISK AND CONCENTRATIONS OF CREDIT RISK

OFF-BALANCE-SHEET RISK

The Credit Union is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its members and to reduce its own exposure to fluctuations in interest rates. These financial instruments include commitments to extend credit. These instruments involve, to varying degrees, elements of credit and interest-rate risk in excess of the amount recognized in the statements of financial condition.

Commitments to extend credit are agreements to lend to a member as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses. Since many of the commitments may expire without being fully drawn upon, the total commitment amounts do not necessarily represent future cash requirements. As of December 31, 2012, total unfunded commitments under such lines of credit approximated $141,300,000. The Credit Union evaluates each member's creditworthiness on a case-by-case basis. The amount of collateral obtained, if any, is based on management's credit evaluation of the member.

CONCENTRATIONS OF CREDIT RISK

A significant amount of the Credit Union's business activity is with members who are employees or former employees of Farmers. The Credit Union also may be exposed to credit risk from a regional economic standpoint, since a significant concentration of its borrowers work or reside in the state of California. However, the loan portfolio is well diversified and the Credit Union does not have any significant concentration of credit risk, except unsecured loans, which by their nature, increase the risk of loss compared to those loans that are collateralized.

NOTE 9: REGULATORY CAPITAL

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

Note 9: (continued)

Quantitative measures established by regulation to ensure capital adequacy require the Credit Union to maintain minimum amounts and ratios (set forth in the table below) of net worth (as defined in NCUA's Regulations) to total assets (as defined in NCUA's Regulations). Credit unions are also required to calculate a Risk-Based Net Worth Requirement (RBNWR) which establishes whether or not the Credit Union will be considered "complex" under the regulatory framework. The Credit Union's RBNWR as of December 31, 2012 and 2011 was 5.26% and 5.09%, respectively. The minimum requirement to be considered complex under the regulatory framework is 6.00%. Management believes, as of December 31, 2012, that the Credit Union meets all capital adequacy requirements to which it is subject.

As of December 31, 2012, the most recent call reporting period, the NCUA categorized the Credit Union as "*well capitalized"* under the regulatory framework for prompt corrective action. To be categorized as "*well capitalized"* the Credit Union must maintain a minimum net worth ratio of 7.00% of assets. There are no conditions or events since that notification that management believes have changed the Credit Union's category.

The Credit Union's actual and required net worth amounts and ratios are as follows:

	As of December 31, 2012		As of December 31, 2011	
	Amount	**Ratio/ Requirement**	**Amount**	**Ratio/ Requirement**
Actual net worth	$77,118,494	12.64%	$72,500,581	12.44%
Amount needed to be classified as "adequately capitalized"	$36,616,349	6.00%	$34,966,986	6.00%
Amount needed to be classified as "well capitalized"	$42,719,074	7.00%	$40,794,817	7.00%

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

Note 10: (continued)

The following tables set forth by level, within the fair value hierarchy, the Credit Union's financial instruments at fair value:

	Assets at Fair Value as of December 31, 2012			
	Level 1	**Level 2**	**Level 3**	**Total**
Assets:				
Mortgage-backed securities	$—	$2,798,878	$—	$2,798,878
NCUA guaranteed notes	—	22,120,195	—	22,120,195
Collateralized-mortgage obligations	—	62,417	—	62,417
	$—	$24,981,490	$—	$24,981,490

	Assets at Fair Value as of December 31, 2011			
	Level 1	**Level 2**	**Level 3**	**Total**
Assets:				
Mortgage-backed securities	$—	$3,133,425	$—	$3,133,425
NCUA guaranteed notes	—	27,423,806	—	27,423,806
Collateralized-mortgage obligations	—	55,896	—	55,896
	$—	$30,613,127	$—	$30,613,127

The estimated fair value amounts have been determined using available market information and appropriate valuation methodologies. However, considerable judgment is required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented are not necessarily indicative of amounts that could be realized in a market exchange. The use of different assumptions and estimation methodologies may have a material effect on the estimated fair value amounts. The following methods and assumptions were used to estimate fair value of each of the financial instruments for which it is practicable to estimate.

CASH
The carrying amount is a reasonable estimation of fair value.

INVESTMENTS
Estimated fair values for investments are obtained from quoted market prices where available.

LOANS TO MEMBERS, NET
The fair value of loans was estimated by discounting the estimated cash flows using market-based assumptions for expected prepayment rates, default rates, loss severity, and required rates of return.

ACCRUED INTEREST RECEIVABLE
The carrying amount is a reasonable estimation of fair value.

Note 10: (continued)

MEMBERS' SHARES AND DEPOSITS

The estimated fair value of demand deposit accounts is the carrying amount. The fair value of fixed-rate certificates was estimated by discounting the estimated cash flows using the current rate at which similar certificates would be issued.

INTEREST PAYABLE

The carrying amount is a reasonable estimation of fair value.

COMMITMENTS TO EXTEND CREDIT

The fair value of commitments to extend credit is equivalent to the amount of credit extended since the Credit Union does not charge fees to enter into these commitments and the commitments are not stated at fixed rates.

The carrying value and estimated fair value of the Credit Union's financial instruments are as follows:

	As of December 31, 2012		As of December 31, 2011	
	Carrying Amount	**Fair Value**	**Carrying Amount**	**Fair Value**
Financial assets:				
Cash	$2,261,269	$2,261,269	$2,022,738	$2,022,738
Investments:				
Available-for-sale	$24,981,490	$24,981,490	$30,613,127	$30,613,127
Held-to-maturity	$27,529,465	$27,529,465	$11,692,000	$11,692,000
Other	$55,766,973	$55,766,973	$50,366,217	$50,366,217
Loans to members, net	$481,127,580	$484,278,355	$472,678,960	$459,466,093
Accrued interest receivable:				
Investments	$69,065	$69,065	$31,930	$31,930
Loans	$2,344,591	$2,344,591	$2,446,012	$2,446,012
Financial liabilities:				
Members' shares and deposits	$527,632,525	$528,934,269	$503,717,346	$505,436,537
Interest payable	$303,636	$303,636	$333,828	$333,828
Unrecognized financial instruments:				
Commitments to extend credit	$—	$141,300,000	$—	$123,723,000

FARMERS INSURANCE GROUP FEDERAL CREDIT UNION
NOTES TO THE FINANCIAL STATEMENTS

NOTE 11: INDUSTRY EVENTS

In January 2009, the NCUA informed federally-insured credit unions that it was taking actions to enhance and support the corporate credit union system as well as the NCUSIF. During June 2009, legislation was created to establish a Temporary Corporate Credit Union Stabilization Fund (Stabilization Fund) to absorb the corporate stabilization costs by borrowing money from the U.S. Treasury. During September 2010, the NCUA received approval from the U.S. Treasury to extend the life of the Stabilization Fund to June 2021. The funds borrowed from the U.S. Treasury will be repaid from assessments authorized by the NCUA Board. The NCUA Board has levied assessments during 2009, 2010, 2011 and 2012 to repay borrowed funds to the U.S. Treasury. It is anticipated that the NCUA Board will be making annual assessments over the next several years to cover costs associated with the corporate credit union system.

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Farmers Insurance Group
Federal Credit Union

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