Puerto Rico Federal Credit Union

# FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT

For the years ended
December 31, 2022 and 2021

Puerto Rico Federal Credit Union

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**INDEPENDENT AUDITORS' REPORT**

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## INDEPENDENT AUDITORS' REPORT

The Supervisory Committee and Board of Directors
Puerto Rico Federal Credit Union
Guaynabo, Puerto Rico

**AUDITORS' OPINION**

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

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Credit Union as of December 31, 2022 and 2021, and the results of its operations, changes in members' equity, comprehensive income and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

**BASIS FOR OPINION**

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

**MANAGEMENT'S RESPONSIBILITIES FOR THE FINANCIAL STATEMENTS**

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error. In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Credit Union's ability to continue as a going concern within one year after the date that the financial statements are available to be issued.

**AUDITOR'S RESPONSIBILITIES FOR THE AUDIT OF THE FINANCIAL STATEMENTS**

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

## REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

In performing an audit in accordance with generally accepted auditing standards, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Credit Union's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Credit Union's ability to continue as a going concern for a reasonable period of time.

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

San Juan, Puerto Rico
March 17, 2023

Llavona Casas, CPA PSC

Stamp No. E-507932
was affixed to the original.

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Puerto Rico Federal Credit Union
**STATEMENTS OF FINANCIAL CONDITION**
December 31, 2022 and 2021

| **Assets** | **2022** | **2021** |
|---|---|---|
| Cash, cash equivalents and restricted cash | $ 30,277,084 | $ 68,431,425 |
| Certificates of deposits | 6,839,268 | 4,361,268 |
| Loans to members, net allowance for loan losses | 108,709,812 | 90,934,467 |
| Investment securities available for sale | 35,786,605 | 37,429,498 |
| Investment securities held to maturity | 2,476,324 | - |
| Accrued interest receivable | 480,574 | 432,726 |
| NCUSIF deposit | 1,748,482 | 1,677,351 |
| Investment in corporate credit union | 1,148,382 | 1,071,520 |
| Property and equipment, net | 5,507,799 | 5,646,494 |
| Foreclosed and repossessed assets | 116,926 | 7,500 |
| Prepaid expenses and other assets | 623,335 | 488,310 |
| Total assets | $ 193,714,591 | $ 210,480,559 |
| **Liabilities and Members' Equity** | | |
| Members' shares and savings accounts | $ 172,893,769 | $ 182,287,823 |
| Accrued interest payable | 58,909 | 55,055 |
| Accounts payable and accrued liabilities | 1,059,173 | 2,863,283 |
| Total liabilities | 174,011,851 | 185,206,161 |
| **Members' Equity** | | |
| Regular reserve | 2,947,255 | 2,947,255 |
| Undivided earnings | 24,986,706 | 23,453,585 |
| Accumulated other comprehensive loss | (8,231,221) | (1,126,442) |
| Total members' equity | 19,702,740 | 25,274,398 |
| Total liabilities and members' equity | $ 193,714,591 | $ 210,480,559 |

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

Puerto Rico Federal Credit Union
**STATEMENTS OF INCOME AND EXPENSES**
For the years ended December 31, 2022 and 2021

| | 2022 | 2021 |
|---|---|---|
| Interest Income: | | |
| Interest on loans | $ 5,111,337 | $ 5,118,195 |
| Interest on investment securities and savings | 1,039,490 | 729,300 |
| Total interest income | 6,150,827 | 5,847,495 |
| Interest expense: | | |
| Interest and dividends on members' shares, savings accounts and borrowed funds | (1,148,901) | (1,205,503) |
| Net interest income | 5,001,926 | 4,641,992 |
| Provision for loan losses | (813,903) | (134,755) |
| Net interest income after provision for loan losses | 4,188,023 | 4,507,237 |
| Service fee and non-interest income | 2,582,351 | 2,198,413 |
| Non-Interest expenses: | | |
| Compensation and benefits | 1,653,340 | 1,529,993 |
| Office operations | 987,024 | 757,542 |
| Occupancy and related | 930,573 | 730,584 |
| Professional services and contracted services | 492,035 | 596,363 |
| Education and promotional | 194,089 | 230,159 |
| Data Processing | 181,799 | 171,200 |
| Loss on disposal of assets | 8,611 | 9,964 |
| Other | 789,782 | 460,861 |
| Total non-interest expenses | 5,237,253 | 4,486,666 |
| **Net Income** | $ 1,533,121 | $ 2,218,984 |

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

**STATEMENTS OF CHANGES IN MEMBERS' EQUITY**

For the years ended December 31, 2022 and 2021

| | Regular Reserve | Undivided Earnings | Accumulated Other Comprehensive Income/(loss) | Total |
|---|---|---|---|---|
| Balance, December 31, 2020 | $ 2,947,255 | $ 21,234,601 | $ 189,841 | $ 24,371,697 |
| Net income | - | 2,218,984 | - | 2,218,984 |
| Other comprehensive income | - | - | (1,316,283) | (1,316,283) |
| Balance, December 31, 2021 | 2,947,255 | 23,453,585 | (1,126,442) | $ 25,274,398 |
| Net income | - | 1,533,121 | - | 1,533,121 |
| Other comprehensive income | - | - | (7,104,779) | (7,104,779) |
| Balance, December 31, 2022 | $ 2,947,255 | $ 24,986,706 | $ (8,231,221) | $ 19,702,740 |

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

Puerto Rico Federal Credit Union
**STATEMENTS OF COMPREHENSIVE INCOME**
For the years ended December 31, 2022 and 2021

| | 2022 | 2021 |
|---|---|---|
| Net Income | $ 1,533,121 | $ 2,218,984 |
| Other Comprehensive income: | | |
| Changes in net unrealized (loss) gain on investment securities available for sale during the year | (7,104,779) | (1,316,283) |
| Total comprehensive (loss) income | $ (5,571,658) | $ 902,701 |

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

Puerto Rico Federal Credit Union
**STATEMENTS OF CASH FLOWS**
For the years ended December 31, 2022 and 2021

| | 2022 | 2021 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net income | $ 1,533,121 | $ 2,218,984 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 276,461 | 295,514 |
| Provision for possible loan losses | 813,903 | 134,755 |
| Loss on disposition of assets | 8,611 | 9,964 |
| Loss (gain) on sale of investment securities | - | (81,227) |
| Premium amortization and discount accretion, net | 12,441 | 18,509 |
| Net unamortized deferred origination fees | (16,967) | (26,791) |
| Recoveries on charged-off loans | 255,064 | 230,847 |
| (Increase) decrease in assets: | | |
| Accrued interest receivable | (47,848) | (58,001) |
| Prepaid expenses and other assets | (135,025) | (161,243) |
| (Decrease) increase in liabilities: | | |
| Accrued interest payable | 3,854 | (19,939) |
| Accounts payable and accrued liabilities | (1,804,109) | 2,189,822 |
| Total adjustments | (633,615) | 2,532,210 |
| Net cash provided by operating activities | 899,506 | 4,751,194 |
| Cash flows from investing activities: | | |
| Cash proceeds from maturities, disposition and return on principal over investments | (10,374,984) | 6,711,601 |
| Net (increase) decrease in certificates of deposit | (2,478,000) | 1,310,011 |
| Adquisition of investment securities available for sale | 3,228,646 | (20,618,589) |
| Net (increase) decrease in loans to members | (18,827,345) | 151,818 |
| Acquisitions of property and equipment | (146,377) | (190,342) |
| Investment in credit corporate union | (71,131) | (364,636) |
| Deposit in NCUSIF | (936,601) | 326,043 |
| Net cash (used) by investing activities | (29,605,792) | (12,674,094) |
| Cash flows from financing activities: | | |
| Net (decrease) increase in shares and savings accounts | (9,448,055) | 38,067,970 |
| Net cash (used) provided by financing activities | (9,448,055) | 38,067,970 |
| Net (decrease) increase in cash, cash equivalents and restricted cash | (38,154,341) | 30,145,070 |
| Cash, cash equivalents and restricted cash at beginning of year | 68,431,425 | 38,286,355 |
| Cash, cash equivalents and restricted cash at end of year | $ 30,277,084 | $ 68,431,425 |

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

**Supplemental Disclosures of Cash Flow Information**

Interests and dividends paid for the years ended December 31, 2022 and 2021 were approximately $1,148,901 and $1,205,504, respectively.

Also, during the years ended December 31, 2022 and 2021, unrealized (loss) on securities available for sale were recognized for ($8,231,221) and ($1,126,442), respectively.

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

## 1. ORGANIZATION

Puerto Rico Federal Credit Union ("Credit Union") is located in Guaynabo Puerto Rico and was organized and chartered under the Federal Credit Union Act ("The Law"). The Credit Union is organized to promote thrift among its members by receiving savings from its members in the form of shares and deposits to provide sources of financing. Its powers are limited to those granted in its regulations and the Law. The Credit Union is governed by the rules established in its statutes and the regulations issued by the National Credit Union Administration (NCUA), the regulatory entity. As of December 31, 2022, and 2021, the NCUA insured the Credit Union shares members' accounts up to $250,000.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements are presented following the accounting principles generally accepted in the United States of America (U.S. GAAP). The most significant policies are as follows:

### Use of Estimates

The preparation of the financial statements in conformity with U.S. GAAP requires management to make certain 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 revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change include the determination of the allowance for loan losses.

### Reclassifications

Certain figures in the accompanying 2021 financial statements were reclassified to conform to the 2022 presentation.

### Concentrations of Credit Risk

Financial instruments that potentially subject the Credit Union to credit risk include cash balances and certificate of deposits with several financial institutions located in Puerto Rico and the United States, which were insured for up to $250,000 by the U.S. Federal Deposit Insurance Corporation (FDIC). The balances may exceed amounts insured by the FDIC. Credit risk for loans receivable and share accounts are also concentrated since most of the Credit Union's members are located in the Puerto Rico geographical area.

### Cash and Cash Equivalents

For purposes of the cash flow statements, the Credit Union considers cash and cash equivalents, the change fund, current accounts in local banks, money market accounts and certificates of deposit that have a maturity date of three months or less from the date of purchase. Certificates of deposit with a maturity date in excess of 90 days from the date of purchase are presented in a separate line in the statement of financial condition.

**Restricted Cash**

The Credit Union adopted the ASU 2016-18 Accounting Standard, to identify its restricted cash in the statement of financial condition and in the statement of cash flows. Restricted cash is an asset that is reserved for a particular purpose primarily to satisfy regulatory or contractual requirements. Restricted assets subject to these specific requirements are segregated from other assets to mark clear boundaries of their use.

**Investment Securities**

Investments are made in accordance with the Credit Union's policies, which incorporate the regulations of National Credit Union Administration (NCUA), hence they are principally in federally sponsored and guaranteed financial instruments. Investment securities are classified and accounted for as investments available-for-sale or held to maturity, according to the requirements of ASC 320, *Accounting for Certain Investments in Debts and Equity Securities*. Interest income is recorded on an accrual basis. In addition, management evaluates individually all investments to determine if any decrease in market value is temporary or not. Any non-temporary decrease is reflected in earnings of the current period and the carrying value of the investment is reduced.

Investment securities held-to-maturity

Investment securities held-to-maturity are those which the management has the intent to hold to maturity. These investments are reported at cost, adjusted for amortization of premiums or accretion of discounts, which are recognized in investment interest income using the effective interest method over the period of maturity. Any permanent reduction in the net realizable value of these investments below their cost is recognized as a loss charged to earnings. Gains and losses on the sale of investments are recognized using the specific cost of each investment.

Investment securities available-for-sale

Investment securities available-for-sale are presented at fair market value. Unrealized gains and losses on securities available for sale are excluded from earnings and recognized as an increase or decrease in other comprehensive income. Investment securities in this classification could be sold any time in response to economic and strategic factors.

Other than temporary decline in the fair market value

Declines in the fair value of held to maturity and available for sale securities below their cost that are other than temporary are reflected as realized losses. In estimating other than temporary impairment, management considers, among others: (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near term prospects of the issuer, (3) that the Credit Union does not intend to sell these securities, and (4) it is more likely than not that the Credit Union will have the ability to hold the securities for a period of time sufficient to allow for any anticipated recovery in fair value.

**Loans to Members and Allowance for Loan Losses**

*Loans to Members*

The Credit Union extends credit to its members through personal loans, auto loans, mortgages, credit cards and lines of credit. During 2022 and 2021, the Credit Union originated loans with an aggregated dollar value of approximately $53,637,000 and $24,570,000, respectively. Loans are stated at the amount of unpaid principal, reduced by an allowance for loan losses and net origination fees. Interest on loans to members is recognized over the terms of the loans and is calculated on principal amounts outstanding.

The accrual of interest on loans is discontinued at the time the loan is 60 days delinquent unless the credit is well-secured and in the process of collection. Past due status is based on contractual terms of the loan. In all cases, loans are placed on non-accrual or charged-off at an earlier date if collection of principal or interest is considered doubtful. All interest accrued but not collected for loans that are placed on nonaccrual or charged-off is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

*Deferred Loan Origination Costs*

Certain direct loan origination costs are deferred and recognized as an adjustment to interest income over the contractual life of the loans.

*Allowance for loan losses*

The allowance for loan losses (allowance) is an estimate of loan losses inherent in the Credit Union's loan portfolio. The allowance is established through a provision for loan losses which is charged to expense. Loan losses are charged-off against the allowance when the Credit Union determines the loan balance to be uncollectible. Cash received on previously charged-off amounts is recorded as a recovery to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic assessment of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

For purposes of determining the allowance, the Credit Union has segmented certain loans in the portfolio by product type. Loans are divided into the following segments: personal loans, auto loans, mortgages, credit cards and lines of credit. The Credit Union further disaggregates these segments into classes based on the associated risks within those segments. Consumer loans are divided into secured and unsecured. The allowance for loan losses is established through a provision for loan losses charged to expenses. Loans are charged against the allowance for loan losses when management believes that the collectability of the principal is unlikely. The recoveries of balances previously charged to the allowance for loan losses are credited to the allowance.

The allowance consists of specific and general components. The specific component covers impaired loans and troubled debt restructurings and the specific allowances are established for these loans based on a thorough analysis of the most probable source of repayment, including the present value of the loan's expected future cash flows, the loan's estimated market value, or the estimated fair value of the underlying collateral. The general component covers non-impaired loans and is based on historical losses adjusted for current factors. This actual loss experience is adjusted for economic factors based on the risks present for each portfolio segment or class of loans. These economic factors include consideration of the following: levels of and trends in delinquencies and impaired loans; levels of and trends in charge-offs and recoveries; trends in volume and terms of loans; effects of any changes in risk selection and underwriting standards; other changes in lending policies, procedures, and practices; experience, ability, and depth of lending management and other relevant staff; national and local economic trends and conditions; industry conditions; and effects of changes in credit concentrations. These factors are inherently subjective and are driven by the repayment risk associated with each portfolio segment. The Credit Union maintains a separate general valuation allowance for each portfolio segment.
These portfolio segments include consumer (unsecured and secured personal loans, auto, credit cards and lines of credit) and mortgage, and with risk characteristics described as follows:

<u>*Consumer*</u>: The consumer loan portfolio usually comprises a large number of small loans, including automobile and personal loans. Most loans are made directly for consumer purchases. Economic trends determined by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans. Weak economic trends indicate the borrowers' capacity to repay their obligations may be deteriorating.

Mortgage: The degree of risk in residential mortgage lending depends primarily on the loan amount in relation to collateral value, the interest rate, and the borrower's ability to repay in an orderly fashion. These loans generally possess a lower inherent risk of loss than other real estate portfolio segments.

*Impaired Loans*

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

*Troubled Debt Restructurings*

Under certain circumstances, the Credit Union will provide borrowers relief through loan restructurings. A loan restructuring represents a troubled debt restructuring (TDR) if for economic or legal reasons related to the borrower's financial difficulties the Credit Union grants a concession to the borrower that it would not otherwise consider. Restructured loans typically present an elevated level of credit risk as the borrowers are not able to perform according to the original contractual terms. Loans that are reported as TDRs are considered impaired and measured for impairment as described above.

*Loan Charge-off Policies*

The Credit Union's quality control process includes preparing lists to monitor and track delinquent loans. Tracking the loans on these lists enables management to assess the performance of the loan portfolio and act to mitigate risk therein through necessary changes in policy and procedures. The quality control process also serves as a tool to assist the Credit Union in identifying loans for charge-off on a timely basis. All loans will be charged-off once deemed uncollectible.

Generally, non-performing loans are deemed to be a loss when they become three months delinquent unless it is determined prior that there is no collectability based on the established loan life collections process. This process includes well defined procedures and guidelines used to identify, monitor, and address non-performing loans and when they should be considered for charge-off.

**Accounts Receivable**

Accounts receivable are stated at their net realizable value.

**Property and Equipment**

Property and equipment are stated at cost, less accumulated depreciation. Depreciation and amortization are computed using the straight-line- method over the estimated useful lives of the assets. Land is stated at cost. Assets classified as construction in process are not depreciated until the asset has been completed and placed into service. Expenditures for maintenance and repairs are charged to operations as incurred. The cost and related accumulated depreciation are eliminated from the accounts when assets are disposed. Any resulting gain or loss is reflected in the results of operations.

**Impairment of Long-Lived Assets**

The Credit Union periodically reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. No indications of impairment are evident at December 31, 2022 and 2021.

**NCUSIF Deposit**

The deposit in the National Credit Union Share Insurance Fund (NCUSIF) is accordance with National Credit Union Administration (NCUA) regulations, requiring the maintenance of a deposit by each insured credit union in an amount equal to one percent (1%) of its insured shares. The deposit would be refunded to the credit union if: (1) the insurance coverage is terminated, (2) The Credit Union converts to insurance coverage from another source; (3) the operations of the fund are transferred from the NCUA Board.

**Assets Acquired in Liquidation of Loans**

Assets acquired in liquidation of loans represent collateral used to secure members' loans that have been acquired by the Credit Union in an effort to settle the members' loan and are recorded at the lower of cost or market less costs of sale. Upon acquisition, the Credit Union determines fair value of the collateral and any losses are charged-off through the allowance for loan losses. The Credit Union continues to review the properties for subsequent impairment and any subsequent declines in fair value are recorded through current period earnings.

**Operating Leases**

Lease contracts, which were identified as operating leases, are recognized in the statement of financial position as "Right-Of-Use assets" (ROU) and in liabilities as "Lease liabilities", for those with terms longer than one year. Lease liabilities and their corresponding "ROU" assets are initially recorded based on the present value of future lease payments, during the expected term of the lease. An incremental borrowing rate is used, which is the rate that is incurred to borrow on a guaranteed basis, over a similar term in an amount equal to the lease payments. The ROU asset could include the initial direct costs paid for the lease and any incentives paid to the lessor. During the year ended December 31, 2022, most leases were classified as operating and, as a result, a lease expense was recognized within operating expenses. Leased property, which includes various rent payments made during the lease term and that are not based on a rate or index, are excluded from the measurement of "ROU" assets and lease liabilities and are recognized as lease expense as incurred.

**Members' Shares Accounts**

The dividend rates are set by the Credit Union's Board of Directors based on an evaluation of current and future market conditions. Dividends on members' shares accounts are based on available earnings at the end of the corresponding period and are not guaranteed by the Credit Union. Dividends are credited to the members' share accounts on the last day of the month for which dividends are declared. Members share accounts are subordinated to all other liabilities of the Credit Union upon liquidation.

**Members' Equity**

Puerto Rico Federal Credit Union is required by regulation to maintain a statutory reserve ("Regular reserves"); representing a regulatory restriction of members' equity, and thus these regular reserves are not available for the payment of dividends on share accounts. The statutory reserve consists of $2,947,255 for both years 2022 and 2021. Other appropriated members' equity amounts may be established or transferred at the discretion of the Board of Directors.

**Comprehensive Income**

Accounting principles generally require revenue, expenses, gains and losses to be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on investment securities, are reported as separate component of members' equity in the statements of financial condition.

**Advertising and Promotional Costs**

Advertising and promotional costs are included in education and promotional expense and are expensed as incurred.

**Federal and State Income Taxes**

The Credit Unions is exempt, by statute, from federal and state income taxes.

**New Accounting Update Not Yet Adopted**

*Measurement of Credit Losses on Financial Instruments.* In June 2016, the Financial Accounting Standards Board (FASB) issued ASU No. 2016-13 Credit Losses (Topic 326-Financial Instruments), which includes an impairment model known as the current expected credit loss model (CECL), that is based on expected losses rather than incurred losses. Under the new guidance, an entity recognizes as an allowance its estimate of expected credit losses based on the lifetime losses of loans portfolios adjusted by prospective qualitative factors. The new standard is effective for the Credit Union for annual periods in fiscal years beginning after December 15, 2022, that is, for fiscal year 2023 (an additional one-year deferral was proposed due to coronavirus pandemic). As of December 31, 2022, the Credit Union have developed various CECL models and is ready for implementation beginning on January 1, 2023.

ASU No. 2022-02, *Troubled Debt Restructurings and Vintage Disclosures*, Topic 326 (Financial Instruments-Credit Losses) – This standard eliminates the accounting guidance for troubled debt restructurings by creditors under Subtopic 310-40, Receivables-Troubled Debt Restructurings by Creditors, requires an entity evaluate whether the modification represents a new loan or a continuation of an existing loan. The amendments to the standard also enhance existing disclosure requirements, and introduce new requirements related to certain modifications of receivables made to borrowers experiencing financial difficulty. For entities that have adopted ASU No. 2016- 13, this new standard is effective for financial statements issued for annual periods beginning after December 15, 2022. The Credit Union does not anticipate the adoption of this standard will have a material impact on the consolidated financial statements.

## 3. BUSINESS COMBINATION

During the month of April 2021, the Credit Union entered into a Merger Agreement ("the Agreement") with two Community Federal Credit Unions. Under the terms of the Agreement, the Credit Union acquired all assets, rights, and property and assume all liabilities of $4,293,738 & $17,166,224 respectively.

The applicable provisions of Accounting Standards Codification ("ASC") 805, "Business Combinations" and the operations of the merged entities are included with the Credit Union's consolidated balances as of the effective dates of acquisition. Under this guidance, the assets acquired, and liabilities assumed for credit union merger are recorded at their respective fair values at the effective date of the merger. If the fair value of the acquired liabilities exceeds the fair value of the acquired assets, then goodwill is recorded; however, if fair value of assets acquired exceeds the fair value of liabilities assumed and entity value acquired, then the difference is recognized in the Credit Union's income statement- other non-interest income- as a merger purchase gain.

Refer to below table for details of the assets acquired and liabilities assumed at fair value.

| **Fair value of Assets Acquired** | **Credit Union 1** | **Credit Union 2** | **Total** |
|---|---|---|---|
| Loans to members, net | $ 1,756,718 | $ 7,031,060 | $ 8,787,778 |
| Cash and cash equivalents | 2,347,884 | 9,592,554 | 11,940,438 |
| Investment securities | 187,541 | 504,072 | 691,613 |
| Property and equipment, net | - | - | - |
| Accrued interest receivable | 1,595 | 14,335 | 15,930 |
| Other assets | - | 24,204 | 24,204 |
| **Fair value of Liabilities Acquired** | | | |
| Members' shares and savings accounts | (4,117,605) | (15,822,021) | (19,939,626) |
| Accounts payable and accrued liabilities | (4,800) | (43,824) | (48,624) |
| Residual Merger Gain | $ 171,333 | $ 1,300,380 | $ 1,471,713 |

## 4. CASH AND CASH EQUIVALENTS

As of December 31, 2022, and 2021, the balance of cash, cash equivalents and restricted cash consisted of the following:

| | **2022** | **2021** |
|---|---|---|
| Operating accounts | $ 21,954,362 | $ 60,707,142 |
| Savings and money market accounts | 7,314,169 | 6,778,911 |
| Change fund and petty cash | 867,961 | 807,495 |
| Total cash and cash equivalents | $ 30,136,492 | $ 68,293,548 |
| Restricted cash | 140,592 | 137,877 |
| Total cash, cash equivalents and restricted cash | $ 30,277,084 | $ 68,431,425 |

The Bank deposits are insured by the Federal Deposit Insurance Corporation (FDIC) and National Credit Union Association (NCUA) up to $250,000 per institution. At December 31, 2022 and 2021, the bank balance of deposits in commercial banks amounting to approximately $21,094,494 and $59,757,619, respectively, exceeded the amounts covered by federal depository insurance limits. There was no bank balance of deposits exceeding the NCUA depository insurance limits at December 31, 2022 and 2021 and the balance of deposits in *Banco Cooperativo* amounting to approximately $1,349,721 and $1,087,443 and were uninsured at December 31, 2022 and 2021, respectively.

**Restricted Cash**

The Credit Union adopted the ASU 2016-18 Accounting Standard, to identify its restricted cash in the statement of financial condition and in the statement of cash flows. Restricted cash is an asset that is reserved for a particular purpose primarily to satisfy regulatory or contractual requirements. Restricted assets subject to these specific requirements are segregated from other assets to mark clear boundaries of their use. As of December 31, 2022, and 2021, the Credit Union had deposited $140,592 and $137,877, respectively, in restricted cash for the payment of property taxes and insurance on properties that serve as collateral under mortgage loans.

## 5. CERTIFICATES OF DEPOSITS

As of December 31, 2022, and 2021, the Credit Union maintains certificates of deposits mostly in denominations of equal or less than $250,000. The schedules maturities at the end of period were as follows:

| | 2021 | 2021 |
|---|---|---|
| Due in one year or less | $ 997,000 | $ 748,000 |
| Due after one year through three years | 3,687,279 | 1,205,278 |
| Due after three years through five years | 2,154,989 | 2,407,990 |
| Total certificates of deposits | $ 6,839,268 | $ 4,361,268 |

## 6. LOANS

As of December 31, 2022, and 2021, the portfolio of loans to members of the Credit Union by type was as follows:

| | 2022 | 2021 |
|---|---|---|
| Loans | | |
| Personal | 32,084,580 | 31,368,455 |
| Auto | 59,457,091 | 40,547,025 |
| Mortgage | 14,231,861 | 15,871,354 |
| Credit cards | 4,146,128 | 4,177,710 |
| Lines of credit | 254,606 | 359,142 |
| Total consumer | 110,174,266 | 92,323,686 |
| Total loans | $ 110,174,266 | $ 92,323,686 |
| Less: Allowance for loan losses | (1,322,291) | (1,230,089) |
| Less: Net unamortized deferred origination fees | (142,163) | (159,130) |
| Total loans to members, net | $ 108,709,812 | $ 90,934,467 |

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method at December 31, 2022 and 2021:

**2022**

| | Personal | Auto | Mortgage | Credit Cards | Lines of Credit | Total |
|---|---|---|---|---|---|---|
| Beginning balance | $ 620,088 | $ 339,489 | $ 172,987 | $ 94,920 | $ 2,605 | $ 1,230,089 |
| Loans charge-offs | 601,559 | 252,383 | - | 122,822 | - | 976,764 |
| Recoveries of loans previously reserved | 79,771 | 156,189 | 336 | 18,768 | - | 255,064 |
| Provision during the year | 541,388 | 214,162 | (107,360) | 167,069 | (1,357) | 813,902 |
| Ending Balance | 541,389 | $ 457,457 | $ 65,963 | $ 157,935 | $ 1,248 | $ 1,322,291 |
| Evaluation of allowance: | | | | | | |
| Allowance evaluated individually | $ 57,360 | $ 5,664 | $ - | $ 4,926 | $ - | $ 67,950 |
| Allowance evaluated collectively | 582,391 | 451,792 | 65,963 | 153,009 | 1,186 | 1,254,341 |
| Total | $ 639,751 | $ 457,456 | $ 65,963 | $ 157,935 | $ 1,186 | $ 1,322,291 |
| Loan ending Balance: | | | | | | |
| Evaluated individually for impariment | $ 130,523 | $ 14,018 | $ 1,399,591 | $ 19,705 | $ - | $ 1,563,837 |
| Evaluated collectivelly for impariment | 31,954,057 | 59,443,073 | 12,832,270 | 4,126,423 | 254,606 | 108,610,429 |
| Total | $ 32,084,580 | $ 59,457,091 | $ 14,231,861 | $ 4,146,128 | $ 254,606 | $ 110,174,266 |

**2021**

| | Personal | Auto | Mortgage | Credit Cards | Lines of Credit | Total |
|---|---|---|---|---|---|---|
| Beginning balance | $ 695,319 | $ 453,456 | $ 168,413 | $ 95,109 | $ 4,032 | $ 1,416,329 |
| ALL aquired by mergers | 60,646 | 48,233 | 29,868 | 3,243 | 2,567 | 144,557 |
| Loans charge-offs | 490,082 | 159,514 | - | 46,852 | - | 696,448 |
| Recoveries of loans previously reserved | 80,892 | 113,993 | - | 36,011 | - | 230,896 |
| Provision during the year | 273,313 | (116,679) | (25,294) | 7,409 | (3,994) | 134,755 |
| Ending Balance | $ 620,088 | $ 339,489 | $ 172,987 | $ 94,920 | $ 2,605 | $ 1,230,089 |
| Evaluation of allowance: | | | | | | |
| Allowance evaluated individually | $ 71,688 | $ 4,881 | $ 59,070 | $ 4,253 | $ - | $ 139,892 |
| Allowance evaluated collectively | 548,400 | 334,608 | 113,917 | 90,668 | 2,604 | 1,090,197 |
| Total | $ 620,088 | $ 339,489 | $ 172,987 | $ 94,921 | $ 2,604 | $ 1,230,089 |
| Loan ending Balance: | | | | | | |
| Evaluated individually for impariment | $ 113,532 | $ 20,901 | $ 1,708,651 | $ 17,010 | $ - | $ 1,860,094 |
| Evaluated collectivelly for impariment | 31,254,923 | 40,526,124 | 14,162,703 | 4,160,700 | 359,142 | 90,463,592 |
| Total | $ 31,368,455 | $ 40,547,025 | $ 15,871,354 | $ 4,177,710 | $ 359,142 | $ 92,323,686 |

Loans to members in which the accrual of interest has been discontinued or reduced amounted to $202,481 and $427,488 at December 31, 2022 and 2021, respectively. If interest on those had been accrued, such income would have approximately $14,000 and $21,000, respectively.

The following table presents the aging of the recorded investment in past due loans at December 31, 2022 and 2021:

**Age Analysis of Loan to members Receivables by Category as of December 31, 2022**

| **December 31, 2022** | Current | 60-90 | 91-120 | Over 121 | Total | Non Accruing |
|---|---|---|---|---|---|---|
| Personal | $ 31,943,402 | $ 141,178 | $ - | $ - | $ 32,084,580 | $ 141,178 |
| Auto | 59,443,073 | 14,018 | - | - | 59,457,091 | 14,018 |
| Mortgage | 14,204,281 | - | - | 27,580 | 14,231,861 | 27,580 |
| Credit cards | 4,126,423 | 19,705 | - | - | 4,146,128 | 19,705 |
| Lines of credit | 254,606 | - | - | - | 254,606 | - |
| Total loans to members | $ 109,971,785 | $ 174,901 | $ - | $ 27,580 | $ 110,174,266 | $ 202,481 |

**Age Analysis of Loan to members Receivables by Category as of December 31, 2021**

| **December 31, 2021** | Current | 60-90 | 91-120 | Over 121 | Total | Non Accruing |
|---|---|---|---|---|---|---|
| Personal | $ 31,254,924 | $ 113,531 | $ - | $ - | $ 31,368,455 | $ 113,531 |
| Auto | 40,526,123 | 20,902 | - | - | 40,547,025 | 20,902 |
| Mortgage | 15,595,309 | - | - | 276,045 | 15,871,354 | 276,045 |
| Credit cards | 4,160,700 | 17,010 | - | - | 4,177,710 | 17,010 |
| Lines of credit | 359,142 | - | - | - | 359,142 | - |
| Total loans to members | $ 91,896,198 | $ 151,443 | $ - | $ 276,045 | $ 92,323,686 | $ 427,488 |

**Credit Quality Information**

**Consumer Loans** - The use of risk classifications in consumer loans allows management to estimate their exposure to different types of risk. The Credit Union has established policies to evaluate application for loans using FICO credit scores, among other information, provided by major credit reporting agencies. A FICO score is a credit score developed by a third party that take information and analyze it to predict consumer behavior, such as how likely someone is to pay their bills on time or not, or whether they are able to handle a larger credit line. Generally, the FICO score range is 300 to 850, with the higher number representing less risk to the lender.

**Credit Quality Levels, Credit Score and Loans to Members' Risk Exposure**

The different levels of risk of loss established internally by the Credit Union according to the FICO credit scores are as follows:

**Level 1** - 720 or more, member has little or no additional risk.

**Level 2** - 719 to 670, member represents a nominal risk of loss.

**Level 3** – 669 -620 or less, member is experiencing some degree of financial difficulty, and represents a potential risk of loss.

**Level 4 -** 619 or less, member represents a high degree of risk of loss.

These levels are reviewed periodically, as well as other statistics and external factors, to monitor the performance of the portfolio.

The following table represents the recorded investment in consumer loans based on FICO score for the years ended December 31, 2022 and 2021:

**2022**

| | FICO SCORE | | | | |
|---|---|---|---|---|---|
| | Over 720 | 719-670 | 669-620 | 619 or less | Total |
| Personal | $ 18,490,708 | $ 8,100,061 | $ 3,455,275 | $ 2,038,536 | $ 32,084,580 |
| Auto | 47,062,925 | 7,548,438 | 2,637,963 | 2,207,765 | 59,457,091 |
| Mortgage | 8,658,796 | 2,806,061 | 544,803 | 2,222,201 | 14,231,861 |
| Credit Cards | 1,777,149 | 1,290,945 | 581,680 | 496,354 | 4,146,128 |
| Lines of Credit | 116,094 | 78,626 | 35,375 | 24,511 | 254,606 |
| Total | $ 76,105,672 | $ 19,824,131 | $ 7,255,096 | $ 6,989,367 | $110,174,266 |

**2021**

| | FICO SCORE | | | | |
|---|---|---|---|---|---|
| | Over 720 | 719-670 | 669-620 | 619 or less | Total |
| Personal | $ 19,245,469 | $ 7,420,435 | $ 3,096,217 | $ 1,606,334 | $ 31,368,455 |
| Auto | 28,809,799 | 6,444,555 | 2,986,483 | 2,306,188 | 40,547,025 |
| Mortgage | 10,800,709 | 2,109,242 | 1,517,910 | 1,443,493 | 15,871,354 |
| Credit Cards | 1,893,586 | 1,192,356 | 606,810 | 484,958 | 4,177,710 |
| Lines of Credit | 140,892 | 148,641 | 47,884 | 21,725 | 359,142 |
| Total | $ 60,890,455 | $ 17,315,229 | $ 8,255,304 | $ 5,862,698 | $ 92,323,686 |

Loan impairment is measured by estimating the expected future cash flows or by valuing the underlying collateral. The following table presents loans individually evaluated for impairment by class of loans as of December 31, 2022 and 2021:

| | Impaired Loans by Category for the year ended December 31, 2022 | | Impaired Loans by Category for the year ended December 31, 2021 | |
|---|---|---|---|---|
| | Unpaid Principal of Impaired Loans (cases) | Specific Associated Allowance for the Impaired Loan (Cases) | Unpaid Principal of Impaired Loans (cases) | Specific Associated Allowance for the Impaired Loan (Cases) |
| Consumer: | | | | |
| Personal | $ 141,178 | $ 57,360 | $ 113,531 | $ 71,688 |
| Auto | 14,018 | 5,664 | 20,902 | 4,881 |
| Mortgage | 27,580 | - | 276,045 | 59,070 |
| Credit cards | 19,705 | 4,926 | 17,010 | 4,252 |
| Total | $ 202,481 | $ 67,950 | $ 427,488 | $ 139,891 |

The following table presents the restructured loans by category as of December 31, 2022 and 2021:

| | For the year ended December 31, 2022 | | | | | |
|---|---|---|---|---|---|---|
| | Restructured Loans | | | Delinquent Loans | | |
| | Loans Count | Principal Balance | Assigned Allowance | Loans Count | Principal Balance | Assigned Allowance |
| Consumer: | | | | | | |
| Personal | 6 | $ 24,485 | $ - | - | $ - | $ - |
| Total | 6 | $ 24,485 | $ - | - | $ - | $ - |

| | For the year ended December 31, 2021 | | | | | |
|---|---|---|---|---|---|---|
| | Restructured Loans | | | Delinquent Loans | | |
| | Loans Count | Principal Balance | Assigned Allowance | Loans Count | Principal Balance | Assigned Allowance |
| Consumer: | | | | | | |
| Personal | 12 | $ 82,088 | $ 20,522 | - | $ - | $ - |
| Total | 12 | $ 82,088 | $ 20,522 | - | $ - | $ - |

**Loans to Related Parties**

Certain officers, directors, and employees had loans with the Credit Union during 2022 and 2021. Such loans were in the ordinary course of business at normal credit terms including interest rates and collateralization and do not represent more than a normal risk of collection. Total loans outstanding to these related parties at December 31, 2022 and 2021, amounted to $839,921 and $871,318, respectively. The following table presents the movement of the loans to related parties during the years ended December 31, 2022 and 2021, and shares collateralizing such loans at December 31, 2022 and 2021:

| | 2022 | 2021 |
|---|---|---|
| Beginning balance of loans | $ 871,318 | $ 691,212 |
| Originations | 217,560 | 511,106 |
| Collections | (248,957) | (331,000) |
| Ending balance of loans | 839,921 | 871,318 |
| Shares | $ 476,050 | $ 1,059,034 |

## 7. INVESTMENT SECURITIES

At December 31, 2022 and 2021 the investment securities available for sale and held to maturity are as follows:

| | 2022 | 2021 |
|---|---|---|
| Investment securities: | | |
| Available for sale | $ 35,786,605 | $ 37,429,498 |
| Held to maturity | 2,476,324 | - |
| | 38,262,929 | 37,429,498 |

As of December 31, 2022 and 2021, the amortized cost and the estimate fair market value of investment securities available for sale were as follows:

**2022**

**Available for sale:**

| Type of Investment | Amortized Cost | Unrealized Gain | Unrealized Loss | Market Value |
|---|---|---|---|---|
| Federal Agriculture Mortgage Corpotation (FAMCA) | $ 504,333 | $ - | $ (152,558) | $ 351,775 |
| Federal Farm Credit Bank (FFCB) | 15,470,911 | - | (3,138,037) | 12,332,874 |
| Federal Home Loan Bank (FHLB) | 6,046,396 | - | (1,369,822) | 4,676,574 |
| Federal Home Loan Mortgage Corporation (FHLMC) | 3,472,763 | - | (867,768) | 2,604,995 |
| Federal National Mortgage Association (FNMA) | 2,069,554 | - | (398,378) | 1,671,176 |
| Mortgage Back Securities Pools (MBS) | 5,686,462 | - | (1,009,657) | 4,676,805 |
| Municipal Bonds | 7,310,309 | - | (1,185,488) | 6,124,821 |
| US Treasury Bonds | 3,457,097 | - | (109,513) | 3,347,585 |
| Total | $ 44,017,825 | $ - | $ (8,231,221) | $ 35,786,605 |

**2022**

**Held to maturity:**

| Type of Investment | Amortized Cost | Unrealized Gain | Unrealized Loss | Market Value |
|---|---|---|---|---|
| Federal Home Loan Bank (FHLB) | 1,982,301 | - | (103,351) | 1,878,950 |
| US Treasury Bonds | 494,023 | - | (939) | 493,085 |
| Total | $ 2,476,324 | $ - | $ (104,290) | $ 2,372,035 |

**2021**

**Available for sale:**

| Type of Investment | Amortized Cost | Unrealized Gain | Unrealized Loss | Market Value |
|---|---|---|---|---|
| Federal Home Loan Bank (FHLB) | $ 5,043,614 | $ - | $ (168,181) | $ 4,875,433 |
| Federal Home Loan Mortgage Corporation (FHLMC) | 3,470,970 | - | (142,930) | 3,328,040 |
| Federal National Mortgage Association (FNMA) | 2,066,571 | - | (55,062) | 2,011,509 |
| Federal Agriculture Mortgage Corpotation (FAMCA) | 504,667 | - | (26,022) | 478,645 |
| Federal Farm Credit Bank (FFCB) | 13,973,764 | 3,718 | (293,956) | 13,683,526 |
| Mortgage Back Securities Pools (MBS) | 6,279,007 | 43,831 | (357,819) | 5,965,019 |
| Municipal Bonds | 7,217,346 | 37,697 | (167,718) | 7,087,326 |
| Total | $ 38,555,939 | $ 85,246 | $ (1,211,688) | $ 37,429,498 |

During the year ended December 31, 2021, the Credit Union had no investments originally held to maturity. The investments on December 31, 2021, were classified as available for sale based on management's intent and ability to hold the securities to maturity.

The amortized cost and estimated fair value of investment securities at December 31, 2022 and 2021, by contractual maturity, are shown below. Investment expected maturities may differ from original contractual maturities because of borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

| | 2022 | | 2021 | |
|---|---|---|---|---|
| **Due Date** | Amortized Cost | Market Value | Amortized Cost | Market Value |
| Due in one year or less | $ 1,481,456 | $ 1,457,095 | $ - | $ - |
| Due in one to five years | 12,140,374 | 11,247,154 | 4,243,902 | 4,229,130 |
| Due after five years through ten years | 20,214,760 | 16,170,035 | 17,722,509 | 17,387,703 |
| Due more than ten years | 12,657,559 | 9,284,356 | 16,589,528 | 15,812,665 |
| Total | $ 46,494,149 | $ 38,158,640 | $ 38,555,939 | $ 37,429,498 |

Unrealized losses as of December 31, 2022 and 2021 have not been recognized into income because they are not considered to be other-than temporary. Management considers the unrealized losses to be market driven, rather than credit driven and no loss will be realized unless the securities are sold.

| | As of December 31, 2022 | | | | | |
|---|---|---|---|---|---|---|
| | Continuing Unrealized Losses for Less Than 12 months | | Continuing Unrealized Losses for 12 months or More | | Total | |
| Description of Securities | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| Federal Agriculture Mortgage Corpotation (FAMCA) | $ - | $ - | $ 351,775 | $ (152,558) | $ 351,775 | $ (152,558) |
| Federal Farm Credit Bank (FFCB) | - | - | 12,332,874 | (3,138,037) | 12,332,874 | (3,138,037) |
| Federal Home Loan Bank (FHLB) | - | - | 6,555,524 | (1,473,173) | 6,555,524 | (1,473,173) |
| Federal Home Loan Mortgage Corporation (FHLMC) | - | - | 2,604,995 | (867,768) | 2,604,995 | (867,768) |
| Federal National Mortgage Association (FNMA) | - | - | 1,671,177 | (398,378) | 1,671,177 | (398,378) |
| Mortgage Back Securities Pools (MBS) | - | - | 4,676,805 | (1,009,657) | 4,676,805 | (1,009,657) |
| Municipal Bonds | - | - | 6,124,821 | (1,185,488) | 6,124,821 | (1,185,488) |
| US Treasury Bonds | 964,010 | (23,423) | 2,876,659 | (87,029) | 3,840,669 | (110,452) |
| | $ 964,010 | $ (23,423) | $ 37,194,630 | $ (8,312,088) | $ 38,158,640 | $ (8,335,511) |

| | As of December 31, 2021 | | | | | |
|---|---|---|---|---|---|---|
| | Continuing Unrealized Losses for Less Than 12 months | | Continuing Unrealized Losses for 12 months or More | | Total | |
| Description of Securities | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| Federal Home Loan Bank (FHLB) | $ - | - | $ 4,875,433 | $ (168,181) | $ 4,875,433 | $ (168,181) |
| Federal Home Loan Mortgage Corporation (FHLMC) | - | - | 3,328,040 | (142,930) | 3,328,040 | (142,930) |
| Federal National Mortgage Association (FNMA) | - | - | 2,011,509 | (55,062) | 2,011,509 | (55,062) |
| Federal Agriculture Mortgage Corpotation (FAMCA) | - | - | 478,645 | (26,022) | 478,645 | (26,022) |
| Federal Farm Credit Bank (FFCB) | - | - | 13,683,526 | (290,238) | 13,683,526 | (290,238) |
| Mortgage Back Securities Pools (MBS) | - | - | 5,965,019 | (313,988) | 5,965,019 | (313,988) |
| Municipal Bonds | - | - | 7,087,326 | (130,021) | 7,087,326 | (130,021) |
| | $ - | $ - | $ 37,429,498 | $ (1,126,442) | $ 37,429,498 | $ (1,126,442) |

## 8. ACCRUED INTEREST RECEIVABLE

At December 31, 2022 and 2021, the following were the components of accrued interest receivable:

| | 2022 | 2021 |
|---|---|---|
| Accrued interests on loans | $ 284,909 | $ 277,232 |
| Accrued interests on investments | 195,665 | 155,494 |
| Total accrued interest receivable | $ 480,574 | $ 432,726 |

## 9. INVESTMENT IN CORPORATE CREDIT UNION

As of December 31, 2022, and 2021, the balance of the investment in the Corporate One Federal Credit Union & Alloya Corporate Federal Credit Union was $1,148,382 and $1,071,520, respectively. This deposit is not subject to the insurance of the National Credit Union Insurance Fund or other deposit insurance.

## 10. PROPERTY AND EQUIPMENT

As of December 31, 2022, and 2021, the property and equipment was composed of the following:

| | Useful Life (in Years) | 2022 | 2021 |
|---|---|---|---|
| Buildings | 40 | $ 3,718,620 | $ 3,708,120 |
| Furniture and fixtures | 1-10 | 1,004,773 | 957,616 |
| Vehicle | 5 | 14,500 | 14,500 |
| Information systems | 3-5 | 1,627,840 | 1,547,731 |
| | | 6,365,733 | 6,227,967 |
| Less accumulated depreciation and amortization | | (4,210,721) | (3,934,260) |
| | | 2,155,012 | 2,293,707 |
| Land | | 3,352,787 | 3,352,787 |
| Total property and equipment | | $ 5,507,799 | $ 5,646,494 |

Depreciation and amortization expense for the years ended December 31, 2022 and 2021, was approximately $276,461 and $295,514, respectively, and is included in occupancy and related expense.

## 11. OTHER ASSETS

As of December 31, 2022 and 2021 the other assets were composed of the following:

| | 2022 | 2021 |
|---|---|---|
| Prepaid expenses | 289,404 | 289,624 |
| Deposits and security bonds | 46,398 | 46,398 |
| Accounts receivable | 10,731 | 71,691 |
| Right of use asset | 160,936 | - |
| Others | 115,866 | 80,597 |
| Total other assets | $ 623,335 | $ 488,310 |

## 12. MEMBERS' SHARES ACCOUNTS

As of December 31, 2022 and 2021 members' shares accounts are summarized as follows:

| | Weighted-Average Dividend Rate at December 31 | | 2022 | | 2021 |
|---|---|---|---|---|---|
| Shares drafts | 0.10% | $ | 4,749,104 | $ | 4,805,567 |
| Regular shares | 0.28% | | 117,646,837 | | 115,273,579 |
| Christmas and summer clubs | 1.00% | | 8,207,764 | | 16,129,783 |
| Share certificates | 1.53% | | 42,290,064 | | 46,078,894 |
| Total members shares accounts | | $ | 172,893,769 | $ | 182,287,823 |

At December 31, 2022, scheduled maturities of share certificates are as follows:

| Year ending December 31, | Amount |
|---|---|
| 2023 | $ 19,385,285 |
| 2024 | 12,545,847 |
| 2025 | 6,274,743 |
| 2026 | 2,373,588 |
| 2027 | 1,293,501 |
| Thereafter | 417,100 |
| | $ 42,290,064 |

Share and deposit amounts up to $250,000 per ownership interest are federally insured through the National Credit Union Share Insurance Fund. Individual deposit account balances exceeding $250,000 at December 31, 2022 and 2021, totaled $7,508,576 and $7,657,350, respectively.

At December 31, 2022 and 2021, interest expense on members' shares, savings accounts and borrowed funds is summarized as follows:

| Type | | 2022 | | 2021 |
|---|---|---|---|---|
| Regular shares | $ | 363,792 | $ | 325,318 |
| Share drafts | | 4,552 | | 4,575 |
| Christmas and summer clubs | | 156,642 | | 108,050 |
| Share certificates | | 623,915 | | 767,560 |
| Total interest expense on members' shares and savings | | 1,148,901 | | 1,205,503 |

## 13. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

As of December 31, 2022 and 2021 the composition of accruals and other liabilities is as follows:

| | 2022 | 2021 |
|---|---|---|
| Accrued payroll and related | $ 74,165 | $ 134,245 |
| Accrued liabilities | 28,672 | 40,852 |
| Accounts payable | 489,407 | 2,234,154 |
| Auto loan registration | 26,013 | 8,842 |
| Escrow accounts | 140,592 | 137,877 |
| Lease liability | 160,936 | - |
| Other | 139,388 | 307,313 |
| Total accruals and other liabilities | $ 1,059,173 | $ 2,863,283 |

## 14. SERVICE FEE AND NON-INTEREST INCOME

Service fee and non-interest income for the years ended December 31, 2022 and 2021 are as follows:

| | 2022 | 2021 |
|---|---|---|
| ATM card fees | $ 185,293 | $ 170,364 |
| Share draft fees | 20,726 | 17,135 |
| ACH fees | 21,393 | 16,473 |
| Credit card fees | 118,624 | 109,941 |
| Late charges | 107,584 | 111,658 |
| Dormant account charges | 29,168 | 36,345 |
| Mortgage origination fees | 16,966 | 28,011 |
| Loan refinancing fees | 12,900 | 10,075 |
| Overdraft fees | 3,531 | 3,346 |
| Gain on sale of investment securities | - | 81,227 |
| Income federal programs "Grants" | 1,826,342 | - |
| Residual merger gain | - | 1,471,713 |
| Miscellaneous | 239,824 | 142,125 |
| Total service fee and non-interest income | $ 2,582,351 | $ 2,198,413 |

## 15. NON-INTEREST EXPENSES

The detail of non-interest expenses for the years ended December 31, 2022 and 2021 were as follows:

| | 2022 | 2021 |
|---|---|---|
| Compensation and benefits | $ 1,653,340 | $ 1,529,993 |
| Office operations | 987,024 | 757,542 |
| Occupancy and related: | | |
| Depreciation and amortization | 276,461 | 295,514 |
| Utilities | 72,507 | 8,481 |
| Insurance | 164,990 | 152,549 |
| Repairs and maintenance | 166,290 | 109,683 |
| Security | 250,325 | 164,357 |
| | 930,573 | 730,584 |
| Professional services and contracted services | 492,035 | 596,363 |
| Education and promotional | 194,089 | 230,159 |
| Data processing | 181,799 | 171,200 |
| Loss on disposal of assets | 8,611 | 9,964 |
| Other operating expenses: | | |
| Credit reports and collection | 166,828 | 104,414 |
| Annual meeting | 77,723 | 28,753 |
| Federal operating | 36,507 | 33,468 |
| Equipment and software maintenance | 341,398 | 187,217 |
| Directors and committee | 31,098 | 18,908 |
| Dues and subscriptions | 17,685 | 16,926 |
| Armored services | 23,525 | 19,591 |
| Other miscellaneous | 95,018 | 51,584 |
| Total other operating expenses | 789,782 | 460,861 |
| Total non-interest expenses | $ 5,237,253 | $ 4,486,666 |

## 16. EMPLOYEE BENEFIT PLAN

The Credit Union maintains a 401k employee benefit plan that substantially covers all of its employees. A Credit Union makes contributions to the plan as follows (1) the Credit Union will make a match of employee contributions up to a maximum of 3% of their basic salary. In addition, the Credit Union will provide half of each additional percent that the employee contributes up to a maximum of 2% of the employee basic salary (2) the Credit Union may make other discretionary contributions of its undivided earnings. During the years ended as of December 31, 2022 and 2021, the Credit Union determined not to contribute additional amounts from their undivided earnings to the employee benefit plan.

During the years ended December 31, 2022 and 2021, Puerto Rico Federal Credit Union contributed $29,399 and $25,895, respectively, to the employee benefit plan.

## 17. UNCERTAINTIES, COMMITMENTS AND CONTINGENCIES

### Fiscal Crisis

The Commonwealth remains amid a profound fiscal crisis affecting the central government and many of its instrumentalities, public corporations and municipalities. This fiscal crisis has been primarily the result of economic contraction, persistent and significant budget deficits, a high debt burden, unfunded legacy obligations, and lack of access to the capital markets, among other factors. As a result of the crisis, the Commonwealth and certain of its instrumentalities have been unable to make debt service payments on their outstanding bonds and notes since 2016. The escalating fiscal and economic crisis and imminent widespread defaults prompted the U.S. Congress to enact the Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA") in June 2016. The Commonwealth and several of its instrumentalities are currently in the process of restructuring their debts through the debt restructuring mechanisms provided by PROMESA.

#### *Exposure of the Credit Union*

The credit quality of Credit Union's loan portfolio reflects, among other things, the general economic conditions in Puerto Rico and other adverse conditions affecting Puerto Rico consumers and businesses. The effects of the prolonged recession have been reflected in limited loan demand, an increase in the rate of foreclosures and delinquencies on loans granted in Puerto Rico. While PROMESA provides a process to address the Commonwealth's fiscal crisis, the length and complexity of the Title III proceedings for the Commonwealth and various of its instrumentalities and the adjustment measures required by the fiscal plans present significant economic risks. In addition, the measures taken to address the fiscal crisis and those that will have to be taken in the near future will likely affect many of our individual customers and customers' businesses, which could cause credit losses that adversely affect us and may negatively affect consumer confidence. This, in turn, could result in reductions in consumer spending that may also adversely impact our interest and non-interest revenues. If global or local economic conditions worsen or the Government of Puerto Rico and the Oversight Board are unable to adequately manage the Commonwealth's fiscal and economic challenges, including by consummating an orderly restructuring of its debt obligations while continuing to provide essential services, these adverse effects could continue or worsen in ways that we are not able to predict.

The accompanying financial statements do not include adjustments related to the effect of the uncertainty related to the Commonwealth's economic conditions and their effects on the Credit Union.

***Interest Rate Risk***

Interest rate risk is the exposure of a credit union current or future revenues and capital to adverse changes in market rates. This risk is a normal part of the risks handled by financial institutions and Credit Unions. The correct management of this risk results in an important source of profitability and value for the Credit Unions; however, excessive interest rate risk can put pressure on revenues, capital, liquidity, and the solvency of the financial institutions. During the year ended December 31, 2022, the effect of the monetary policy of the Federal Reserve Bank, in relation to the speed of increases in interest rates, has put pressure on the balance sheets of the financial institutions in general, specifically on the aforementioned lines. As of December 31, 2022, the Cooperative was closely measuring and monitoring this risk, in order to effectively anticipate and control any adverse effect that may arise on exposure to it.

**Litigation**

Several former employees filed various complaints in Court alleging unjust dismissal of employment, retaliation and other claims. The Credit Union filed its answers to the complaints contending that plaintiffs were justly dismissed from their employment based on the results of an internal audit which revealed violations to policies and procedures established, and other disciplinary actions.  The credit union settled the cases for a minimum amount which were reimbursed by the credit union's insurance.

The Credit Union has no other legal claims that normally are associated with the ordinary operations of a financial institution.

**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. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the statements of financial condition. The contract or notional amounts of those instruments reflect the extent of involvement the Credit Union has in particular classes of financial instruments.

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, 2022, and 2021, the total unfunded commitments under such credit cards and lines-of-credit were approximately $6,780,325 and $8,153,793, respectively. 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.

## 18. FAIR VALUE MEASUREMENTS

GAAP establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement). The three levels of the fair value hierarchy under this guidance are described below:

*Basis of Fair value Measurement*

Level 1 - Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Credit Union has the ability to access at the measurement date. An active market for the asset or liability is a market in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 - Valuation is based on inputs other than quoted market prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. The valuation may be based on quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.

Level 3 - Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. Level 3 assets and liabilities include financial instruments whose value is determined by using pricing models, discounted cash flow methodologies, or similar techniques.
The estimated fair values of the Credit Union's financial statements, none of which are held for trading purposes, are as follows:

| | December 31, 2022 | | December 31, 2021 | |
|---|---|---|---|---|
| | Carrying Amount | Fair Value | Carrying Amount | Fair Value |
| Financial Assets: | | | | |
| Cash and cash equivalents | $ 30,277,084 | $ 30,277,084 | $ 68,431,425 | $ 68,431,425 |
| Certificates of deposits | 6,839,268 | 6,839,268 | 4,361,268 | 4,361,268 |
| Investment securities | 38,262,929 | 35,786,605 | 37,429,498 | 37,429,498 |
| Loans receivable (net of unamortized deferred origination fees) | 110,174,266 | 104,896,216 | 92,323,686 | 87,491,848 |
| Less: allowance for loan losses | (1,322,291) | (1,322,291) | (1,230,089) | (1,230,089) |
| Accrued interest receivable | 480,574 | 480,574 | 432,726 | 432,726 |
| Assets acquired in liquidation of loans | 116,926 | 116,926 | 7,500 | 7,500 |
| | $ 184,828,756 | $ 177,074,382 | $ 201,756,014 | $ 196,924,176 |
| Financial Liabilities | | | | |
| Members' shares accounts | $ 172,893,769 | 172,893,769 | $ 182,287,823 | 182,287,823 |
| Off- Balance Sheet Financial: | | | | |
| Commitments to extend credit | $ 6,780,325 | $ 6,780,325 | $ 8,153,793 | $ 8,153,793 |

## Assets Measured at Fair Value on a Recurring and Non-Recurring Basis

The fair values of assets and liabilities measured on a recurring and nonrecurring basis at December 31, 2022 and 2021 are as follows:

| | | Fair Value Measurement At Reporting Date Using: | | |
|---|---|---|---|---|
| **Asset Class** | **Fair Value** | **Level 1** | **Level 2** | **Level 3** |
| December 31, 2022 | | | | |
| Investment securities | $ 35,786,605 | $ 35,786,605 | - | - |
| Assets acquired in liquidation of loans | $ 116,926 | - | - | $ 116,926 |
| December 31, 2021 | | | | |
| Investment securities | $ 37,429,498 | $ 37,429,498 | - | - |
| Assets acquired in liquidation of loans | $ 7,500 | - | - | $ 7,500 |

## 19. REGULATORY CAPITAL

As of December 31, 2022, and 2021, the Credit Union's net worth to total assets ratio is categorized as "well capitalized" as per the most recent call report. To be categorized as "well capitalized", the Credit Union must maintain a minimum net worth ratio of 7% as defined under the regulatory framework provisions of Section 38 of the FDI Act. Credit Unions whose net worth ratio falls below 7% will be subject to Prompt Corrective Actions requirements.

The Credit Union net worth ratio at December 31, 2022 and 2021 follows:

| | PRFCU Actual | | |
|---|---|---|---|
| Period | Net Worth Amount | Net Worth to Total Assets Ratio (1) | PRFCU Category (2) |
| 2022 | $ 27,933,961 | 14.42% | Well Capitalized |
| 2021 | $ 26,400,840 | 12.54% | Well Capitalized |

(1) In performing its calculation of total assets, the credit union used the monthly average over the quarter option, as permitted by regulation.
(2) There are no conditions or events since the most recent Call Report that management believes have changed the Credit Union's category.

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 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.

**20. SUBSEQUENT EVENTS**

The financial statements and related disclosures include evaluation of events up through and including March 17, 2023, which is the date the financial statements were available to be issued.

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