



4 Old River Place  
 Jackson, Mississippi 39202  
 601.944.4152 Telephone  
 601.944.0808 Fax  
 www.hopecu.org  
 www.hope-ec.org

## Management Discussion and Analysis

### Balance Sheet Analysis

Hope Credit Union's (HCU's) total assets stood at \$178.5 million at December 31, 2014, down just over \$8.2 million from December 31, 2013. This significant drop is entirely due to one transaction. In November, 2013 Hope Enterprise Corporation (HEC), HCU's primary sponsor, closed a New Markets Tax Credit transaction to finance the rehabilitation of a charter school in New Orleans. HCU agreed to be the depository for the two construction accounts related to this transaction which totaled \$17 million. Construction is scheduled to be complete in the summer of 2015. As a result, the total assets of HCU rose rapidly at the end of 2013 and have declined since as draws for construction have been made on these accounts.

As detailed in the following schedule, the vast majority of HCU's assets are tied up in some form of loan or property that resulted from a loan:

	<b>2014</b>	<b>2013</b>
Mortgage loans held-for-sale		57,756,017
Loans receivable – net	127,020,959	60,856,368
Real estate and other assets acquired by foreclosure	1,164,895	1,601,869
<b>Total</b>	<b>128,185,854</b>	<b>120,214,254</b>
<b>Percent of total assets</b>	<b>72%</b>	<b>64%</b>

In 2014 HCU determined that, because of the continued dysfunction in the national secondary residential mortgage markets, its growing portfolio of long-term residential mortgage loans could no longer be classified as held-for-sale as there really were no secondary market purchasers willing to purchase any of the portfolio at a price that HCU would be willing to contemplate. As such, HCU's mortgage portfolio was reclassified as loans held-for-sale to loans receivable along with its consumer and commercial loans.

The reduction in liabilities from \$184.1 million at December 31, 2013 to \$173.9 million at December 31, 2014 was the result of two competing swings. Deposits and members' share accounts declined by \$11.9 million, from \$140.7 million at December 31, 2013 to \$128.8 million at December 31, 2014. The advances from the two construction accounts, discussed earlier, caused a significant portion of the decline, as did a decline in the balance in certificates. To mitigate HCU's interest rate risk inherent in its fixed-rate mortgage portfolio, HCU management has intentionally worked to reduce some of its exposure to short-term certificates and added long-term fixed-rated liabilities. Federal Home Loan Bank advances grew from \$21.7 million at December 31, 2013 to \$24.2 million at December 31, 2014.

Under 12 CFR 701.34(b) low-income designated credit unions (of which HCU is one) may accept secondary capital and can recognize the value of the funds as net worth for regulatory purposes. As such, for regulatory purposes, HCU's net worth was as detailed in the following schedule:

	<b>2014</b>	<b>2013</b>
Secondary capital loans, net of maturity classifications	13,095,000	14,065,500
Regular reserve	10,000	10,000
Undivided profits	4,373,507	2,588,535
Accumulated other comprehensive income (loss)	200,146	(8,658)
<b>Total net worth</b>	<b>17,678,653</b>	<b>16,655,377</b>
<b>Capital ratio</b>	<b>9.91%</b>	<b>8.92%</b>

### Earnings Analysis

Interest income declined in 2014 to \$7.6 million from \$7.8 million in 2013 almost entirely because interest rates remained extremely low and higher earning loans continued to be replaced in the portfolio by low earning loans. The same is true of interest expense where interest expense declined from \$2.5 million in 2013 to \$2.2 million in 2014. In this case, a decline in deposits added to the decline in interest expense related to members' shares and certificates from \$1.3 million in 2013 to \$1.1 million in 2014. However, even though HCU increased its long-term debt, its interest expense related to borrowed funds also dropped from \$1.2 million in 2013 to \$1.1 million in 2014.

The provision for loan losses grew slightly in 2014 to \$902,000 from \$828,000 in 2013. This was primarily a reflection of the growth in the portfolio.

Non-interest income rose dramatically in 2014. Grant and contracts revenue increased to \$6.6 million in 2014 from \$3.6 million, an increase of \$3 million. In August 2014 HCU was awarded a \$2 million Financial Assistant Award and a \$3 million Healthy Food Financing Award from the CDFI Fund of the U.S. Treasury Department. In 2014 Service charges and fees also rose, though not as dramatically, from \$2.5 million to \$2.8 million.

Non-interest expenses increased from \$10.2 million in 2013 to \$12 million in 2014, an increase of \$1.8 million. This increase in expenses was largely the result of an enlarged operating base as HCU opened four additional locations during 2014 and operated locations opened in 2013 for the full year.



Richard Campbell  
Chief Financial Officer



William Bynum  
Chief Executive Officer

# Hope Federal Credit Union

## FINANCIAL STATEMENTS

December 31, 2014 and 2013



**CRI** CARR  
RIGGS &  
INGRAM

CPAs and Advisors

[CRIcpa.com](http://CRIcpa.com) | [blog.cricpa.com](http://blog.cricpa.com)



**Hope Federal Credit Union  
Table of Contents  
December 31, 2014 and 2013**

**TAB: REPORT**

Independent Auditors' Report 1

**TAB: FINANCIAL STATEMENTS**

Statements of Financial Condition 3

Statements of Income 4

Statements of Comprehensive Income (Loss) 5

Statements of Changes in Members' Equity 6

Statements of Cash Flows 7

Notes to Financial Statements 8



Carr, Riggs & Ingram, LLC  
282 Commerce Park Drive  
Ridgeland, MS 39157

Mailing Address:  
P.O. Box 2418  
Ridgeland, MS 39158-2418

(601) 853-7050  
(601) 853-9331 (fax)  
[www.cricpa.com](http://www.cricpa.com)

## **INDEPENDENT AUDITORS' REPORT**

To the Board of Directors of  
Hope Federal Credit Union  
Jackson, Mississippi

We have audited the accompanying financial statements of Hope Federal Credit Union ("Hope"), which comprise the statements of financial condition as of December 31, 2014 and 2013, and the related statements of income, comprehensive income (loss), changes in 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.

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

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

## Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Hope as of December 31, 2014 and 2013, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## Related Party Transactions

The accompanying financial statements have been prepared from the separate accounts maintained by Hope and may not be indicative of the conditions that would have existed or the results of operations that would have occurred had Hope not entered into certain related party transactions with its primary sponsor as described in Note 11 of the notes to the financial statements. Our opinion is not modified with respect to this matter.

*Carr, Riggs & Ingram, L.L.C.*

CARR, RIGGS & INGRAM, LLC

Ridgeland, Mississippi  
April 27, 2015

**Hope Federal Credit Union**  
**Statements of Financial Condition**

<i>December 31,</i>	<b>2014</b>	<b>2013</b>
<b>Assets</b>		
Cash and cash equivalents	\$ 19,527,081	\$ 35,850,309
Short-term investments	1,387,196	2,023,857
Investment securities available-for-sale	17,689,003	16,389,729
Mortgage loans held-for-sale, net	-	57,756,017
Loans receivable, net	127,020,959	60,856,368
Restricted investment securities	1,068,000	995,900
Premises and equipment, net	6,291,870	6,069,908
Accrued interest receivable	547,213	648,623
Receivable from Hope Enterprise Corporation	-	641,427
Grants and other receivables	1,545,506	1,872,616
National Credit Union Share Insurance Fund deposits	1,190,154	1,172,728
Goodwill	244,472	244,472
Real estate and other assets acquired by foreclosure	1,164,895	1,601,869
Prepaid expenses and other assets	799,897	592,140
<b>Total assets</b>	<b>\$ 178,476,246</b>	<b>\$ 186,715,963</b>
<b>Commitments and contingencies (Notes 10, 11, and 14)</b>		
<b>Liabilities and members' equity</b>		
Liabilities:		
Deposits and members' share accounts	\$ 128,834,741	\$ 140,712,700
Accounts payable and accrued expenses	1,405,585	1,908,237
Payable to Hope Enterprise Corporation	23,411	-
Notes payable to financial institution	2,000,000	-
Federal Home Loan Bank advances	24,204,632	21,702,425
Maturity reclassification of secondary capital loans	4,329,224	5,737,224
Secondary capital loans, net of maturity reclassifications	13,095,000	14,065,500
Total liabilities	173,892,593	184,126,086
Members' equity:		
Regular reserve	10,000	10,000
Undivided profits	4,373,507	2,588,535
Accumulated other comprehensive income (loss)	200,146	(8,658)
Total members' equity	4,583,653	2,589,877
<b>Total liabilities and members' equity</b>	<b>\$ 178,476,246</b>	<b>\$ 186,715,963</b>

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

## Hope Federal Credit Union Statements of Income

<i>Years ended December 31,</i>	<b>2014</b>	2013
<b>Interest income</b>		
Interest and fees on loans	\$ 7,144,419	\$ 7,438,218
Interest on securities and interest-bearing accounts	409,893	373,491
 Total interest income	 7,554,312	 7,811,709
<b>Interest expense</b>		
Members' shares and certificates	1,092,821	1,300,248
Borrowed funds	1,128,404	1,193,019
 Total interest expense	 2,221,225	 2,493,267
 Net interest income	 5,333,087	 5,318,442
 Provision for loan losses	 901,688	 827,602
 Net interest income after provision for loan losses	 4,431,399	 4,490,840
<b>Non-interest income</b>		
Grants and contracts revenue	6,604,310	3,586,739
Service charges and fees	2,758,642	2,465,412
Other income	13,221	-
Realized investment losses	(16,004)	(11,219)
 Total non-interest income	 9,360,169	 6,040,932
<b>Non-interest expense</b>		
Employee compensation and benefits	4,960,390	4,471,953
Professional and outside services	1,835,023	1,066,224
Marketing and promotional	204,909	320,090
Office occupancy and operations	3,556,629	2,776,491
Loss from sale and impairments of foreclosed real estate	284,112	180,075
Other	1,165,533	1,385,553
 Total non-interest expense	 12,006,596	 10,200,386
 <b>Net income</b>	 <b>\$ 1,784,972</b>	 <b>\$ 331,386</b>

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

**Hope Federal Credit Union**  
**Statements of Comprehensive Income (Loss)**

<i>Years ended December 31,</i>	<b>2014</b>	2013
<b>Net Income</b>	<b>\$ 1,784,972</b>	\$ 331,386
Other comprehensive income (loss)		
Unrealized gains (losses) on investment securities available for sale:		
Unrealized holding gains (losses) arising during the year	<b>192,800</b>	(432,745)
Reclassification adjustment for losses included in operations	<b>16,004</b>	11,219
Total unrealized losses on securities	<b>208,804</b>	(421,526)
<b>Comprehensive Income (loss)</b>	<b>\$ 1,993,776</b>	\$ (90,140)

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

## Hope Federal Credit Union Statements of Changes in Members' Equity

<i>Years ended December 31, 2014 and 2013</i>	Regular Reserve	Undivided Profits	Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
Balance, January 1, 2013	\$ 10,000	\$ 2,257,149	\$ 412,868	\$ 2,680,017
Net income		331,386		331,386
Change in unrealized gain (loss) on investment securities available for sale			(421,526)	(421,526)
Balance, December 31, 2013	10,000	2,588,535	(8,658)	2,589,877
Net income		<b>1,784,972</b>		<b>1,784,972</b>
Change in unrealized gain (loss) on investment securities available for sale			<b>208,804</b>	<b>208,804</b>
Balance, December 31, 2014	<b>\$ 10,000</b>	<b>\$ 4,373,507</b>	<b>\$ 200,146</b>	<b>\$ 4,583,653</b>

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

## Hope Federal Credit Union Statements of Cash Flows

<i>Years ended December 31,</i>	<b>2014</b>	2013
<b>Operating activities:</b>		
Net income	\$ 1,784,972	\$ 331,386
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation	739,242	720,066
Loss on disposal of premises and equipment	282	-
Investment discount accretions and premium amortizations	94,372	78,116
Realized investment losses	16,004	11,219
Gain on sale of loans held-for-sale	(135,823)	(158,884)
Provision for loan losses	901,688	827,602
Net loan origination costs deferred	(105,073)	(122,317)
Losses on sale and impairments of foreclosed real estate	284,112	180,075
Proceeds from sales of mortgage loans held-for-sale	5,371,157	7,188,665
Originations of mortgage loans held-for-sale	-	(15,393,349)
Purchase of mortgage loans held-for-sale	-	(1,637,227)
Principal collected on mortgage loans held-for-sale	-	4,579,847
Changes in operating assets and liabilities:		
Prepaid expense and other assets	(207,757)	121,099
Accrued interest receivable	101,410	(86,336)
Grants and other receivables	327,110	(1,772,747)
Receivable from primary sponsor	664,838	1,744,943
Accounts payable and accrued expenses	(502,652)	1,007,468
<b>Net cash used in operating activities</b>	<b>9,333,882</b>	<b>(2,380,374)</b>
<b>Investing activities:</b>		
Net change in short-term investments	636,661	(1,507,659)
Purchase of investment securities available-for-sale	(21,465,285)	(7,176,355)
Proceeds from maturities and pay-downs of investment securities available-for-sale	20,264,439	4,583,882
Proceeds from sale of investment securities available-for-sale	-	45,000
Net increase in loans	(16,012,645)	(1,860,258)
Proceeds from sales of foreclosed real estate	1,724,984	1,017,139
Purchase of property and equipment	(961,486)	(454,579)
Purchase of restricted security investment	(72,100)	(117,000)
National Credit Union Insurance Fund deposit increase	(17,426)	(90,791)
<b>Net cash used in investing activities</b>	<b>(15,902,858)</b>	<b>(5,560,621)</b>
<b>Financing activities:</b>		
Net increase in deposits and members' share accounts	(11,877,959)	23,822,348
Repayment of secondary capital loans	(2,378,500)	(1,130,550)
Proceeds from note payable with financial institution	2,000,000	-
Proceeds from Federal Home Loan Bank advances	4,500,000	3,200,000
Repayment of Federal Home Loan Bank advances	(1,997,793)	(1,545,868)
<b>Net cash provided by (used in) financing activities</b>	<b>(9,754,252)</b>	<b>24,345,930</b>
<b>Increase (decrease) in cash and cash equivalents</b>	<b>(16,323,228)</b>	<b>16,404,935</b>
<b>Cash and cash equivalents, beginning of year</b>	<b>35,850,309</b>	<b>19,445,374</b>
<b>Cash and cash equivalents, end of year</b>	<b>\$ 19,527,081</b>	<b>\$ 35,850,309</b>
<b>Supplemental Cash Flow Disclosure:</b>		
Non-cash activity - property received upon foreclosure of loans	\$ 1,572,122	\$ 1,133,754
Interest paid	\$ 2,247,250	\$ 2,512,488

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

## Hope Federal Credit Union Notes to Financial Statements

### NOTE 1: SUMMARY OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES

#### *Nature of Business*

Hope Federal Credit Union (“Hope”) is a chartered cooperative association located in Jackson, Mississippi. Hope operates as a federal chartered organization under the provisions of the Federal Credit Union Act and is organized for the purpose of promoting thrift among and creating a source of credit for its members as defined in its charter and bylaws. Hope has branches in Mississippi, Louisiana, Tennessee and Arkansas and its primary source of revenue results from providing financial services to members and from grants and contractual services from its primary sponsor to support its mission.

Hope's primary sponsor, Hope Enterprise Corporation (“HEC”) operates as a community development financial institution (see Note 10). Under the New Markets Tax Credit Program, which is part of the Community Renewal Tax Relief Act of 2000, HEC invested approximately \$15 million in Hope in the form of grants and secondary capital through an affiliate. Proceeds from this investment are being used to provide an affordable lending program to low-income communities.

#### *Basis of Financial Statement Presentation and Accounting Estimates*

The financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates. The allowance for loan losses and the valuation of investments and foreclosed property are determined utilizing material estimates that are particularly susceptible to change in the near term.

Hope’s financial statements filed with the National Credit Union Administration (“NCUA”) are prepared on the basis of regulatory accounting principles (“RAP”). The following represents the principal differences between the accompanying financial statements prepared in conformity with GAAP and Hope’s financial statements prepared under RAP:

- GAAP requires members’ shares to be classified as liabilities rather than equity as allowed by RAP.
- RAP allows secondary capital accounts in low-income designated credit unions with maturities exceeding five years to be classified as equity (capital) while GAAP requires secondary capital accounts to be classified as liabilities.
- RAP requires placing loans in non-accrual status when they become 90 days or more delinquent which may or may not result in acceptable measurement under GAAP.

**NOTE 1: SUMMARY OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***Cash Equivalents***

Hope considers all highly liquid investments with original maturities of three months or less to be cash equivalents.

***Short-term investments***

Short-term investments include certificates of deposit and other interest bearing accounts with maturities generally less than one year.

***Investment Securities***

Investment securities available-for-sale are carried at fair value. Unrealized gains and losses are reported as part of other comprehensive income or loss. Securities within the available-for-sale portfolio may be used as part of Hope's asset/liability strategy and may be sold in response to changes in interest rate risk, prepayment risk or other similar economic factors. Premiums and discounts on investment securities are recognized as adjustments to interest income by the interest method over the period to maturity and adjusted for prepayments as applicable. The specific identification method is used to compute gains or losses on the sale of these assets. Interest earned on these assets is included in interest income.

When the fair value of a security falls below carrying value, an evaluation must be made to determine if the unrealized loss is a temporary or other than temporary impairment. Impaired securities that are determined to be other than temporarily impaired are written down by a charge to earnings to the extent the impairment is related to credit losses or if the fair value of the security is less than the security's amortized cost basis and Hope intends, or more-likely-than-not will be required, to sell the security before recovery of the security's amortized cost basis. Hope uses a systematic methodology to evaluate potential impairment of its investments and considers, among other things, the magnitude and duration of the decline in fair value, the financial health of and business outlook of the issuer and its ability and intent to retain investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. For a debt security, the difference between the present value of the expected cash flows and the amortized book value is considered a credit loss. When an other than temporary impairment exists for a debt security and Hope does not intend to sell the security or it is more-likely-than-not that it will not be required to sell the security, before recovery of the security's amortized cost basis, the charge to earnings is limited to the amount of credit loss. Any remaining difference between fair value and amortized cost is recognized in other comprehensive income or loss.

***Fair Value Measurements***

Hope carries its investment securities available-for-sale at fair value on a recurring basis and measures certain other assets and liabilities at fair value on a nonrecurring basis using a hierarchy of measurements which requires it to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

**NOTE 1: SUMMARY OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Three levels of inputs are used to measure fair value:

- Level 1** Valuations based on unadjusted quoted prices for identical assets in active markets accessible at the measurement date.
- Level 2** Valuations derived for similar assets in active markets, or other inputs that are observable or can be corroborated by market data.
- Level 3** Valuations derived from unobservable (supported by little or no market activity) inputs that reflect an entity's best estimate of what hypothetical market participants would use to determine a transaction price at the reporting date.

When quoted market prices in active markets are unavailable, Hope determines fair value using various valuation techniques and models based on a range of observable market inputs including pricing models, quoted market price of publicly traded securities with similar duration and yield, time value, yield curve, prepayment speeds, default rates and discounted cash flow. In most cases, these estimates are determined based on independent third party valuation information, and the amounts are disclosed in Level 2 of the fair value hierarchy. Generally, Hope obtains a single price or quote per instrument from independent third parties to assist in establishing the fair value of these investments.

If quoted market prices and independent third party valuation information are unavailable, Hope produces an estimate of fair value based on internally developed valuation techniques, which, depending on the level of observable market inputs, will render the fair value estimate as Level 2 or 3. On occasions when pricing service data is unavailable, Hope may rely on bid/ask spreads from dealers in determining fair value.

Historically, Hope has not experienced a circumstance where it has determined that an adjustment to a quote or price received from an independent third party valuation source is required. To the extent Hope determines that a price or quote is inconsistent with actual trading activity observed in that investment or similar investments, or if management does not believe the quote is reflective of the market value for the investment, Hope would internally develop a fair value using this observable market information and disclose the occurrence of this circumstance.

***Mortgage Loans Held-for-Sale***

Loans held-for-sale consist of mortgage loans that Hope has the intent to sell in the foreseeable future. These loans are carried at the lower of aggregate cost or fair value. Deferred loan fees and costs are reflected in the basis of loans held for sale and, as such, impact the resulting gain or loss when loans are sold. Adjustments to reflect fair value and realized gains and losses upon ultimate sale of the loans are recorded in noninterest income. Net unrealized losses, if any, are recognized

**NOTE 1: SUMMARY OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)**

through a valuation allowance by a charge to operations.

During 2014, Hope transferred its mortgage loans held-for-sale to loans receivable held for investment purposes as a result of increased restrictions in the secondary market for sales of mortgage loans originated with the credit risk characteristics of Hope's typical borrowers. As a result of these increased restrictions, management does not believe the majority of these loans will be sold in the foreseeable future.

Gains and losses on sales of loans are recognized at settlement dates and are determined by the difference between the sales proceeds and the carrying value of the loans. The gain on the sale of mortgage loans held-for-sale was approximately \$135,000 and \$159,000 in 2014 and 2013, respectively. All sales are made without recourse. All mortgage loans are collateralized by the related residence of the borrower.

***Loans Receivable***

Loans are stated at the amount of unpaid principal, adjusted for the net amount of direct costs and nonrefundable fees associated with the lending process, and reduced by the allowance for possible loan losses. Interest on all loans is calculated by the simple interest method on daily balances of the principal amount outstanding. The net amount of nonrefundable loan origination fees and direct costs associated with the lending process is deferred and accreted to interest income over the lives of the loans using a method that approximates the interest method. As of December 31, 2014 and 2013, net deferred origination costs approximated \$663,000 and \$558,000.

Discounts and premiums on purchased loans are amortized to income using a method that approximates the interest method over the remaining period to contractual maturity, adjusted for anticipated prepayments.

The accrual of interest on loans is discontinued when, in the opinion of management, there is an indication that the borrower may be unable to meet payments as they become due, unless the loan is adequately secured. Upon such discontinuance, all unpaid accrued interest is reversed against current income unless the collateral for the loan is sufficient to cover the accrued interest. Interest received on non-accrual loans generally is either applied against principal or reported as interest income, according to management's judgment as to the collectability of principal. The policy for interest recognition on impaired loans is consistent with the nonaccrual interest recognition policy. Generally, loans are restored to accrual status when the obligation is brought current and has performed in accordance with the contractual terms for a reasonable period of time and the ultimate collectability of the total contractual principal and interest is no longer in doubt.

A loan is considered a troubled debt restructuring if the borrower is experiencing financial difficulties and Hope has granted a concession. Concessions may include interest rate reductions or below market interest rates, principal forgiveness, restructuring amortization schedules, reductions in collateral and other actions intended to minimize potential losses.

**NOTE 1: SUMMARY OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***Acquired Loans***

Loans acquired are recorded at fair value with no carryover of the related allowance for credit losses. Fair value of the loans involves estimating the amount and timing of principal and interest cash flows expected to be collected on the loans and discounting those cash flows at a market rate of interest. These loans were aggregated into one pool based upon common risk characteristics. The excess of cash flows expected at acquisition over the estimated fair value is referred to as the accretable discount and is recognized into interest income over the remaining life of the loan. The difference between contractually required payments at acquisition and the cash flows expected to be collected at acquisition is referred to as the nonaccretable difference. The nonaccretable difference includes estimated future credit losses expected to be incurred over the life of the loan.

Subsequent decreases to the expected cash flows will require Hope to evaluate the need for an additional allowance for credit losses. Subsequent improvement in expected cash flows will result in the reversal of a corresponding amount of the nonaccretable difference which will then be reclassified as accretable discount and recognized into interest income over the remaining life of the loan.

***Loan Servicing***

Mortgage loans serviced for others are not included in the accompanying statements of financial condition of Hope. The loans are serviced primarily for the Federal National Mortgage Association, and the unpaid balances approximated \$2,719,000 and \$3,695,000 as of December 31, 2014 and 2013, respectively. The amount of capitalized servicing assets is included in other assets and approximated \$26,000 and \$44,000 as of December 31, 2014 and 2013, respectively.

***Allowance for Loan Losses***

The allowance for possible loan losses is established through a provision for loan losses charged to expenses and is determined based on various components for both individually impaired loans and homogenous pools of loans. Hope evaluates the allowance for possible loan losses on impaired business member loans and certain impaired members mortgage loans on an individual loan basis. All other loans are evaluated on a collective basis. Loans are charged against the allowance for possible loan losses by portfolio segment, net of recoveries, when management believes that the collectability of the principal is unlikely. The methodology for determining charge-offs is consistently applied to each segment. The allowance is an amount management believes will be adequate to absorb possible losses on existing loans that may become uncollectible, based on evaluations of the collectability of loans and prior loan loss experience. The evaluations take into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans, historical trends, and current economic conditions that may affect the borrower's ability to pay. Losses on individually identified impaired member business loans are measured based on the present value of

**NOTE 1: SUMMARY OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)**

expected future cash flows discounted at each loan's original effective market interest rate. As a practical expedient, impairment may be measured based on the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. When the measure of the impaired loan is less than the recorded investment in the loan, the impairment is recorded through the provision added to the allowance for loan losses.

Though management believes the allowance for loan losses to be adequate, ultimate losses may vary from their estimates. However, estimates are reviewed periodically, and, as adjustments become necessary, they are reported in earnings during periods in which they become known.

A loan is considered impaired when, based on current information and events, it is probable that Hope will be unable to collect the scheduled payments of principal and 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 evaluated for impairment consist of nonperforming business loans and include certain internally classified accruing loans. Additionally, during 2014, Hope began evaluating all mortgage loans past due 240 days or greater on an individual loan basis. Large groups of smaller balance member loans, including mortgage loans less than 240 days past due, are collectively evaluated for impairment. Hope does not separately identify individual consumer loans for impairment.

***Restricted Investment Securities***

Restricted investment securities consist of investments in Federal Home Loan Bank stock and are carried at cost.

***Premises and Equipment***

Property and equipment are stated at cost, if purchased, and estimated fair value at the date received, if donated to Hope. Depreciation is provided by the straight-line method over the estimated useful lives of the assets which range from three to thirty-nine years. Hope reviews long-lived assets, including property and equipment, for impairment whenever events or changes in circumstances indicate that the carrying amount of assets may not be recoverable. If the future undiscounted cash flows expected to result from the use of the assets and their eventual disposition are less than the carrying amounts, an impairment loss is recognized.

***Real Estate and Other Assets Acquired by Foreclosure***

Hope records real estate acquired by foreclosure at the lesser of the outstanding loan amount (including accrued interest, if any) or fair value, less estimated costs to sell, at the time of foreclosure. Any resulting loss on foreclosure is charged to the valuation allowance for possible loan losses and a new basis is established in the property. A valuation allowance and a

## Hope Federal Credit Union Notes to Financial Statements

### **NOTE 1: SUMMARY OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)**

corresponding charge to operations is established to reflect declines in value subsequent to acquisition, if any, below the new basis. Required developmental costs associated with foreclosed property under construction are capitalized and considered in determining the fair value of the property. Operating expenses of such properties, net of related income, and gains and losses on their disposition are included in other non-interest expenses.

#### ***National Credit Union Share Insurance Fund Deposit***

The deposit in the National Credit Union Share Insurance Fund (“NCUSIF”) is in accordance with NCUA regulations, which require the maintenance of a deposit by each insured credit union in an amount equal to one percent of its insured shares. The deposit will be refunded to Hope if its insurance coverage is terminated or if it converts to insurance coverage from another source.

#### ***NCUSIF Insurance Premium***

Hope is required to pay an annual insurance premium, unless the payment is waived by the NCUA Board. During 2014, the NCUA waived the annual NCUSIF insurance premium assessment. During 2013, the NCUA Board voted to assess each federally-insured credit union a premium of .080% of its insured shares as of June 30, 2013 to repay a portion of its Temporary Corporate Credit Union Stabilization Fund borrowings from the U.S. Treasury. For Hope, this premium assessment approximated \$94,000 in 2013.

#### ***Deposit and Members’ Share Accounts***

Members’ shares are subordinated to all other liabilities of Hope, excluding secondary capital loans, upon liquidation. Interest on members’ share accounts is based on available earnings at the end of an interest period and is not guaranteed by Hope. Interest rates on members’ share accounts and certificates are set by the Board of Directors, based on an evaluation of current and future market conditions. Members’ shares are insured up to \$250,000 per account through the NCUSIF.

#### ***Income Taxes***

Hope is exempt, by statute, from federal and state income taxes.

#### ***Grant Revenue***

Unconditional grants are recognized as revenue in the period the commitment is received. Conditional grants are recorded as revenue when the conditions of the grant are met unless the likelihood of the condition not being met is remote. As of December 31, 2014 and 2013, grants and other receivables included federally awarded grants of approximately \$821,000 and \$1,347,000, respectively.

**NOTE 1: SUMMARY OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***Comprehensive Income and Loss***

Other comprehensive income or loss is comprised of unrealized gains or losses on investment securities available for sale.

***Advertising Cost***

During 2014 and 2013, Hope had marketing and promotional expenses of approximately \$205,000 and \$320,000, respectively.

***Fair Value Disclosures of Financial Instruments***

The following methods and assumptions were used by Hope to disclose the estimated fair value of each class of financial instruments:

***Cash, Cash Equivalents and Interest-bearing  
Accounts with Corporate Credit Unions***

The carrying amounts reported in the balance sheets for these financial instruments approximate their fair values.

***Investment Securities***

The fair value of investment securities are generally obtained from independent pricing services based upon valuations for similar assets in active markets or other inputs derived from objectively verifiable information.

***Loans Receivable, Including Loans Held-for-Sale***

For variable-rate loans that reprice frequently and have no significant change in credit risk, fair values are based on carrying values. Fair values for certain mortgage loans (for example, one-to-four family residential), credit card loans and other consumer loans are estimated using a discounted cash flow calculation that applies interest rates currently being offered similar loans to a schedule of aggregated expected monthly maturities of borrowers of similar credit quality. Fair values for impaired loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

***Restricted Investment Securities and NCUSIF Deposits***

The carrying amount reported in the balance sheets for these financial instruments approximates their fair values and considers the limited marketability of such securities.

**NOTE 1: SUMMARY OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***Deposits and Members' Shares***

The fair value disclosed for regular share, share draft and money market accounts are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts). The carrying amounts of regular share, share draft and money market accounts approximate their fair values at the reporting date. Fair values for share certificates are estimated using a discounted cash flow calculation that applies interest rates currently being offered on share certificates to a schedule of aggregated expected monthly maturities on Hope's current share certificates.

***Notes Payable to Financial Institution***

The carrying amount reported in the balance sheets for this financial instrument approximates its fair value due to the short-term nature of the borrowing.

***Long-term Debt (including Secondary Capital Loans)***

The fair value of this debt is estimated by discounting the future cash flows using Hope's incremental borrowing rate for similar types of borrowing arrangements as of year end.

***Off-Balance Sheet Instruments***

The fair values of loan commitments and letters of credit approximate the fees currently charged for similar agreements. The fees associated with these financial instruments are immaterial.

***Subsequent Events***

In connection with the preparation of the financial statements, management of Hope evaluated subsequent events through April 27, 2015, which is the date the financial statements were available to be issued.

***Effects of Recent Accounting Guidance***

In January 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-04, *Receivables – Troubled Debt Restructuring by Creditors (Subtopic 310-40): Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure (a consensus of the FASB Emerging Issues Task Force)*. This ASU clarifies when an "in substance repossession or foreclosure" occurs, that is, when a creditor should be considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, such that all or a portion of the loan should be derecognized and the real estate property recognized. ASU 2014-04 states that a creditor is considered to have received physical

**NOTE 1: SUMMARY OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)**

possession of residential real estate property collateralizing a consumer mortgage loan, upon either the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure, or the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. The provisions of ASU 2014-04 also require disclosure of both the amount of foreclosed residential real estate property held by the creditor and the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure. ASU 2014-04 is effective for annual periods beginning after December 15, 2014, and may be applied using either a modified retrospective transition method or a prospective transition method as described in ASU 2014-04. The adoption of ASU 2014-04 is not expected to have a significant impact to Hope's financial statements.

In May 2014, the FASB issued ASU 2014-09, "*Revenue from Contracts with Customers (Topic 606).*" ASU 2014-09 implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps: (i) identify the contract(s) with a customer, (ii) identify the performance obligations in the contract, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract and (v) recognize revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 is effective for the Company on January 1, 2018. The Company is still evaluating the potential impact on Hope's financial statements.

In June 2014, the FASB issued ASU 2014-11, "*Transfers and Servicing (Topic 860).*" ASU 2014-11 requires that repurchase-to-maturity transactions be accounted for as secured borrowings consistent with the accounting for other repurchase agreements. In addition, ASU 2014-11 requires separate accounting for repurchase financings, which entails the transfer of a financial asset executed contemporaneously with a repurchase agreement with the same counterparty. ASU 2014-11 requires entities to disclose certain information about transfers accounted for as sales in transactions that are economically similar to repurchase agreements. In addition, ASU 2014-11 requires disclosures related to collateral, remaining contractual tenor and of the potential risks associated with repurchase agreements, securities lending transactions and repurchase-to-maturity transactions. ASU 2014-11 is effective for Hope on January 1, 2015 and is not expected to have a significant impact on Hope's financial statements.

In January 2015, the FASB issued ASU 2015-01, "*Income Statement - Extraordinary and Unusual Items (Subtopic 225-20) – Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items.*" ASU 2015-01 eliminates from U.S. GAAP the concept of extraordinary items, which, among other things, required an entity to segregate extraordinary items considered to be unusual and infrequent from the results of ordinary operations and show the item separately in the income statement, net of tax, after income from continuing operations. ASU 2015-01 is effective for Hope beginning January 1, 2016, though early adoption is permitted. ASU 2015-01 is not expected to have a significant impact on Hope's financial statements.

## Hope Federal Credit Union Notes to Financial Statements

### NOTE 1: SUMMARY OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### **Reclassifications**

Certain reclassifications have been made to the 2013 financial statements to conform to the 2014 method of presentation.

### NOTE 2: INVESTMENT SECURITIES

The amortized cost and related approximate fair value of investment securities available-for-sale follows:

<i>December 31, 2014</i>	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Debt securities:				
Negotiable certificates of deposits	\$ 1,225,000	\$ -	\$ -	\$ 1,225,000
U.S. Government and federal agencies	7,164,753	40,423	12,157	7,193,019
Municipal obligations	3,021,801	90,872	13,241	3,099,432
Collateralized mortgage obligations	242,484	558	-	243,042
Residential mortgage-backed securities	5,834,819	123,191	29,500	5,928,510
	<b>\$ 17,488,857</b>	<b>\$ 255,044</b>	<b>\$ 54,898</b>	<b>\$ 17,689,003</b>

<i>December 31, 2013</i>				
Debt securities:				
US Treasury securities	\$ 108,593	\$ -	\$ 182	\$ 108,411
U.S. Government and federal agencies	7,605,972	43,936	32,468	7,617,440
Municipal obligations	3,485,908	16,105	44,937	3,457,076
Collateralized mortgage obligations	321,783	406	651	321,538
Residential mortgage-backed securities	4,876,131	95,034	85,901	4,885,264
	<b>\$ 16,398,387</b>	<b>\$ 155,481</b>	<b>\$ 164,139</b>	<b>\$ 16,389,729</b>

**Hope Federal Credit Union**  
**Notes to Financial Statements**

**NOTE 2: INVESTMENT SECURITIES (Continued)**

The amortized cost and related approximate fair value of investment securities available-for-sale at December 31, 2014 by contractual maturity, are as follows:

	<b>Amortized Cost</b>	<b>Fair Value</b>
Due in one year or less	\$ 734,926	\$ 737,720
Due after one year through five years	9,313,988	9,389,043
Due after five years through ten years	7,105,716	7,207,616
Due after ten years	334,227	354,624
	<b>\$ 17,488,857</b>	<b>\$ 17,689,003</b>

For purposes of the maturity table, mortgage-backed securities, which are not due at a single maturity date, have been allocated over maturity groupings based on the weighted-average contractual maturities of underlying collateral. Actual maturities may differ from contractual maturities because of the borrowers' right to call or prepay obligations.

During 2014 Hope recognized gross realized gains and gross realized losses of approximately \$4,000 and \$20,000, respectively, resulting from prepayments of mortgage-backed securities. There were no sales of investment securities available-for-sale during 2014. Gross realized losses during 2013 resulted from the sale of one municipal obligation with gross proceeds of \$45,000 and from prepayments of mortgage-backed securities and approximated \$11,000.

***Temporarily Impaired Securities***

The impairment of available-for-sale debt securities that are in temporarily impaired positions is primarily attributable to interest rates. The length of time temporarily impaired available-for-sale securities have been held in a loss position as of December 31, 2014 and 2013 is summarized below:

	<b>Held Less than 12 Months</b>		<b>Held 12 Months or More</b>		<b>Total</b>	
	<b>Estimated Fair Value</b>	<b>Unrealized Losses</b>	<b>Estimated Fair Value</b>	<b>Unrealized Losses</b>	<b>Estimated Fair Value</b>	<b>Unrealized Losses</b>
December 31, 2014						
U.S. Government and federal agencies	\$ -	\$ -	\$ 504,306	\$ 12,157	\$ 504,306	\$ 12,157
Municipal obligations	254,908	3,021	489,780	10,220	744,688	13,241
Residential mortgage- backed securities	-	-	1,966,110	29,500	1,966,110	29,500
<b>Total</b>	<b>\$ 254,908</b>	<b>\$ 3,021</b>	<b>\$ 2,960,196</b>	<b>\$ 51,877</b>	<b>\$ 3,215,104</b>	<b>\$ 54,898</b>

## Hope Federal Credit Union Notes to Financial Statements

### NOTE 2: INVESTMENT SECURITIES (Continued)

December 31, 2013	Held Less than 12 Months		Held 12 Months or More		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
U.S. Treasury securities	\$ 108,411	\$ 182	\$ -	\$ -	\$ 108,411	\$ 182
U.S. Government and federal agencies	1,313,317	32,468	-	-	1,313,317	32,468
Municipal obligations	864,922	44,937	-	-	864,922	44,937
Collateralized mortgage obligations	302,495	651	-	-	302,495	651
Residential mortgage- backed securities	2,182,586	85,901	-	-	2,182,586	85,901
Total	\$ 4,771,731	\$ 164,139	\$ -	\$ -	\$ 4,771,731	\$ 164,139

### NOTE 3: MORTGAGE LOANS HELD FOR SALE

There were no mortgage loans held for sale as of December 31, 2014.

As of December 31, 2013, mortgage loans held for sale included loans past due 30-89 days of approximately \$4,023,000 and loans 90 days or greater past due, all of which were on non-accrual, of approximately \$6,111,000.

At December 31, 2013, mortgage loans held for sale included loans for which Hope had granted concessions to borrowers and classified as troubled debt restructurings of approximately \$3,314,000. During 2013, Hope granted concessions in the form of loan modifications for 9 loans in which the pre-modified balances outstanding approximated \$609,000 and the post-modified balances approximated \$654,000. There were no specific charge-offs related to troubled debt restructured mortgage loans during 2013. Additionally, during 2013 there were no troubled debt restructured mortgage loans that subsequently defaulted within twelve months of their modification dates.

**Hope Federal Credit Union  
Notes to Financial Statements**

**NOTE 4: LOANS RECEIVABLE**

Loans receivable consist of the following:

<i>December 31,</i>	<b>2014</b>	2013
Member Business Loans:		
Real estate:		
Construction and land development	\$ 2,107,674	\$ 2,036,271
Single family	21,061,466	18,283,891
Commercial	6,610,042	6,326,709
Other	15,634,366	15,708,458
Commercial and industrial	7,638,815	3,196,378
Member Mortgage Loans	62,480,170	-
Member Consumer Loans:		
Secured by automobile loans	6,741,470	9,660,327
Unsecured loans	2,156,087	2,767,811
Secured by share accounts	1,064,438	799,698
Secured by real estate	3,311,425	3,373,486
Other secured consumer loans	176,863	322,310
	<b>128,982,816</b>	62,475,339
Less allowance for loan losses	<b>(1,961,857)</b>	(1,618,971)
	<b>\$ 127,020,959</b>	\$ 60,856,368

***Related Party Loans***

In the ordinary course of business, Hope makes loans to its officers and upper management. The outstanding balance of loans made to such borrowers approximated \$19,000 at December 31, 2014. There was no outstanding balance of loans made to such borrowers at December 31, 2013.

Management believes these loans are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons and did not involve more than normal risk of collectability or present other unfavorable features.

***Loan Concentrations***

Hope grants commercial, real estate and installment loans to its members. Hope does not have any loan concentrations other than as reflected in the preceding summary.

**Hope Federal Credit Union**  
**Notes to Financial Statements**

**NOTE 4: LOANS RECEIVABLE (Continued)**

A summary of the loans and related allowance for possible loan losses evaluated for impairment both individually and collectively at December 31, 2014, was as follows:

<i>December 31, 2014</i>	Loans		Allowance		Net
	Individually	Collectively	Individually	Collectively	
Member Business Loans:					
Real estate:					
Construction and land development	\$ -	\$ 2,107,674	\$ -	\$ 31,615	\$ 2,076,059
Single family	148,963	20,912,503	-	335,438	20,726,028
Commercial	45,897	6,564,145	3,779	133,957	6,472,306
Other	1,752,866	13,881,500	26,668	266,588	15,341,110
Commercial and industrial	608,206	7,030,609	135,693	138,607	7,364,515
Member Mortgage Loans	3,053,663	59,426,507	380,048	295,681	61,804,441
Member Consumer Loans:					
Secured by automobile loans	-	6,741,470	-	36,182	6,705,288
Unsecured loans	-	2,156,087	-	160,812	1,995,275
Secured by share accounts	-	1,064,438	-	7,910	1,056,528
Secured by real estate	-	3,311,425	-	6,497	3,304,928
Other secured consumer loans	-	176,863	-	2,382	174,481
<b>Net Loans</b>	<b>\$ 5,609,595</b>	<b>\$ 123,373,221</b>	<b>\$ 546,188</b>	<b>\$ 1,415,669</b>	<b>\$ 127,020,959</b>

*December 31, 2013*

Member Business Loans:					
Real estate:					
Construction and land development	\$ -	\$ 2,036,271	\$ -	\$ 30,544	\$ 2,005,727
Single family	391,336	17,892,555	22,429	315,573	17,945,889
Commercial	114,897	6,211,812	2,273	137,181	6,187,255
Other	1,740,649	13,967,809	10,761	309,246	15,388,451
Commercial and industrial	433,107	2,763,271	61,832	75,309	3,059,237
Member Consumer Loans:					
Secured by automobile loans	-	9,660,327	-	195,300	9,465,027
Unsecured loans	-	2,767,811	-	115,416	2,652,395
Secured by share accounts	-	799,698	-	2,368	797,330
Secured by real estate	-	3,373,486	-	-	3,373,486
Other secured consumer loans	-	322,310	-	53,138	269,172
Unallocated allowance	-	-	-	287,601	(287,601)
<b>Net Loans</b>	<b>\$ 2,679,989</b>	<b>\$ 59,795,350</b>	<b>\$ 97,295</b>	<b>\$ 1,521,676</b>	<b>\$ 60,856,368</b>

## Hope Federal Credit Union Notes to Financial Statements

### NOTE 4: LOANS RECEIVABLE (Continued)

#### *Impaired and Nonperforming Loans*

In a prior year, Hope acquired certain loans with deteriorated credit quality through business acquisitions. The carrying value of these loans approximated \$97,000 as of December 31, 2014 and \$223,000 as of December 31, 2013 and is included in the balance sheet amounts of consumer automobile loans.

The following is a summary of the changes in the accretable yield on loans acquired through business acquisitions with deteriorated credit quality during 2014 and 2013.

<i>Years ended December 31,</i>	<b>2014</b>	2013
Balance, beginning of year	\$ -	\$ 433,001
Accretion	-	(433,001)
Balance, end of year	\$ -	\$ -

As of December 31, 2014 and 2013, information relative to impaired member business and mortgage loans is as follows:

<i>December 31, 2014</i>	Unpaid Principal Balance	Total Loans with No Specific Allowance	Total Loans with a Specific Allowance	Specific Allowance
Member Business Loans:				
Real estate:				
Single family	\$ 148,963	\$ 148,963	\$ -	\$ -
Commercial	45,897	-	45,897	3,779
Other	1,752,866	999,322	753,544	26,668
Commercial and industrial	608,206	70,208	537,998	135,693
Member Mortgage Loans	3,053,663	1,061,399	1,992,264	380,048
Total impaired loans	\$ 5,609,595	\$ 2,279,892	\$ 3,329,703	\$ 546,188

**Hope Federal Credit Union**  
**Notes to Financial Statements**

**NOTE 4: LOANS RECEIVABLE (Continued)**

<i>December 31, 2013</i>	<b>Unpaid Principal Balance</b>	<b>Total Loans with No Specific Allowance</b>	<b>Total Loans with a Specific Allowance</b>	<b>Specific Allowance</b>
Member Business Loans:				
Real estate:				
Single family	\$ 391,336	\$ 263,160	\$ 128,176	\$ 22,429
Commercial	114,897	66,408	48,488	2,273
Other	1,740,649	913,490	827,159	10,761
Commercial and industrial	433,107	78,960	354,147	61,832
<b>Total impaired loans</b>	<b>2,679,989</b>	<b>1,322,018</b>	<b>1,357,970</b>	<b>97,295</b>

The average recorded investment in impaired loans approximated \$4,145,000 in 2014 and \$2,704,000 in 2013. Interest income recognized on impaired loans approximated \$168,000 in 2014 and \$72,000 in 2013.

***Credit Quality Indicators***

The credit quality indicator utilized by Hope to internally analyze the loan portfolio is the internal risk rating. At the time of loan origination, a risk rating based on an eight point grading system is assigned to each member business loan based on loan officer and management assessments of the risk associated with each particular loan. The first four loan ratings are "pass" rated credits. Loans classified as pass credits have no material weaknesses and are performing as agreed. Loans classified as criticized/especially mentioned have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of Hope's credit position at some future date. Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that Hope will sustain some loss if the deficiencies are not corrected. Loans classified as doubtful have all the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, highly questionable and improbable. Loans classified as loss are considered uncollectible and their continuance as a loan is not warranted.

## Hope Federal Credit Union Notes to Financial Statements

### NOTE 4: LOANS RECEIVABLE (Continued)

The following is a summary of the carrying amount of member business loans by credit quality indicator at December 31, 2014 and 2013:

<i>December 31, 2014</i>	Pass Categories	Especially Mentioned Category	Substandard Category	Doubtful Category	Total
Real estate:					
Construction and land development	\$ -	\$ 2,107,674	\$ -	\$ -	\$ 2,107,674
Single family	6,037,583	14,874,920	-	148,963	21,061,466
Commercial	3,662,933	2,901,212	-	45,897	6,610,042
Other	3,660,147	10,641,538	-	1,332,681	15,634,366
Commercial and industrial	2,436,362	4,594,247	-	608,206	7,638,815
<b>Total member business loans</b>	<b>\$ 15,797,025</b>	<b>\$ 35,119,591</b>	<b>\$ -</b>	<b>\$ 2,135,747</b>	<b>\$ 53,052,363</b>

#### *December 31, 2013*

Real estate:					
Construction and land development	\$ 36,271	\$ 2,000,000	\$ -	\$ -	\$ 2,036,271
Single family	3,500,276	14,392,279	-	391,336	18,283,891
Commercial	2,927,554	3,284,258	-	114,897	6,326,709
Other	3,631,879	10,335,930	-	1,740,649	15,708,458
Commercial and industrial	730,981	2,032,290	-	433,107	3,196,378
<b>Total member business loans</b>	<b>\$ 10,826,961</b>	<b>\$ 32,044,757</b>	<b>\$ -</b>	<b>\$ 2,679,989</b>	<b>\$ 45,551,707</b>

Member mortgage and consumer loans are underwritten using standardized criteria and characteristics. Generally mortgage loans with a member's total debt to gross income ratio exceeding 43% will not be approved. Except for impaired member mortgage loans greater than 240 days past due, which are measured for impairment individually, these loans are normally risk rated and monitored collectively on a monthly basis. These are typically loans to individuals and are delineated as either performing or nonperforming. Performing loans include current and 30 – 89 days past due. Nonperforming loans include loans greater than 90 days past due still accruing and non-accrual loans.

**Hope Federal Credit Union  
Notes to Financial Statements**

**NOTE 4: LOANS RECEIVABLE (Continued)**

<i>December 31, 2014</i>	<b>Consumer Loans</b>		
	<b>Performing</b>	<b>Nonperforming</b>	<b>Total</b>
Member mortgage loans	\$ 54,951,649	7,528,521	\$ 62,480,170
Member consumer loans:			
Secured by automobiles	6,727,068	14,402	6,741,470
Unsecured	2,148,756	7,331	2,156,087
Secured by share accounts	1,056,726	7,712	1,064,438
Secured by real estate	3,294,813	16,612	3,311,425
Other secured consumer loans	176,863	-	176,863
<b>Total loans</b>	<b>\$ 68,355,875</b>	<b>\$ 7,574,578</b>	<b>\$ 75,930,453</b>
 <i>December 31, 2013</i>			
Member consumer loans:			
Secured by automobiles	\$ 9,441,895	\$ 218,432	\$ 9,660,327
Unsecured	2,696,898	70,913	2,767,811
Secured by share accounts	785,705	13,993	799,698
Secured by real estate	3,055,228	318,258	3,373,486
Other secured consumer loans	321,437	873	322,310
<b>Total loans</b>	<b>\$ 16,301,163</b>	<b>\$ 622,469</b>	<b>\$ 16,923,632</b>

**Hope Federal Credit Union  
Notes to Financial Statements**

**NOTE 4: LOANS RECEIVABLE (Continued)**

An aging analysis of past due and nonaccrual loans by class at December 31, 2014 and 2013 was as follows:

<i>December 31, 2014</i>	Current	Past Due 30-89 Days	Past Due Greater Than 90 Days	Nonaccrual	Total
Member Business Loans:					
Real estate:					
Construction and land development	\$ 2,107,674	\$ -	\$ -	\$ -	\$ 2,107,674
Single family	20,912,503	-	-	148,963	21,061,466
Commercial	6,564,145	-	-	45,897	6,610,042
Other	13,881,501	420,184	-	1,332,681	15,634,366
Commercial and industrial	6,774,947	395,662	-	468,206	7,638,815
Member Mortgage Loans	51,491,396	3,460,253	-	7,528,521	62,480,170
Member Consumer Loans:					
Secured by automobiles	6,362,980	364,088	-	14,402	6,741,470
Unsecured	2,107,462	41,294	-	7,331	2,156,087
Secured by share accounts	1,020,922	35,804	-	7,712	1,064,438
Secured by real estate	3,147,531	147,282	-	16,612	3,311,425
Other secured consumer loans	175,990	873	-	-	176,863
<b>Total loans</b>	<b>\$ 114,547,051</b>	<b>\$ 4,865,440</b>	<b>\$ -</b>	<b>\$ 9,570,325</b>	<b>\$ 128,982,816</b>

*December 31, 2013*

Member business loans:					
Real estate:					
Construction and land development	\$ 2,036,271	\$ -	\$ -	\$ -	\$ 2,036,271
Single family	17,315,038	577,517	391,336	-	18,283,891
Commercial	5,745,058	-	114,897	466,754	6,326,709
Other	13,951,073	-	1,504,105	253,280	15,708,458
Commercial and industrial	2,887,614	45,657	78,960	184,147	3,196,378
Member consumer loans:					
Secured by automobiles	8,879,301	562,594	-	218,432	9,660,327
Unsecured	2,557,348	139,550	-	70,913	2,767,811
Secured by share accounts	738,962	46,743	-	13,993	799,698
Secured by real estate	2,949,929	105,299	-	318,258	3,373,486
Other secured consumer loans	317,621	3,816	-	873	322,310
<b>Total loans</b>	<b>\$ 57,378,215</b>	<b>\$ 1,481,176</b>	<b>\$ 2,089,298</b>	<b>\$ 1,526,650</b>	<b>\$ 62,475,339</b>

## Hope Federal Credit Union Notes to Financial Statements

### NOTE 4: LOANS RECEIVABLE (Continued)

There were no loans past due over 90 days and still accruing interest as of December 31, 2014. Accruing loans past due over 90 days and still accruing interest approximated \$2,089,000 as of December 31, 2013.

#### ***Troubled Debt Restructurings***

At December 31, 2014 and 2013, held for investment loans of Hope classified as troubled debt restructurings (TDRs) approximated \$6,303,000 and \$452,000, respectively. Hope had no commitments outstanding to lend additional amounts as of December 31, 2014 and 2013 to borrowers with outstanding loans classified as TDRs. TDRs are evaluated along with impaired loans. For TDRs, Hope had a related loan loss allowance of approximately \$170,000 and \$40,000 at December 31, 2014 and 2013, respectively. There were no specific charge-offs related to TDRs for 2014 or 2013. Additionally, during 2014 and 2013 there were no TDRs that subsequently defaulted within twelve months of their modification dates.

A summary of held for investment loans classified as TDRs outstanding were as follows:

	In Accrual Status		In Non-Accrual Status		Total TDRs Outstanding	
	Number	Amount	Number	Amount	Number	Amount
<i>December 31, 2014</i>						
Member Business Loans:						
Secured by real estate	1	\$ 420,185	2	\$ 918,770	3	\$1,338,955
Not secured by real estate	1	140,000	3	174,113	4	314,113
Member Mortgage Loans	33	3,208,693	15	1,171,306	48	4,379,999
Member Consumer Loans:						
Secured by real estate	5	101,600	1	1,440	6	103,040
Not secured by real estate	19	110,708	5	56,332	24	167,040
<b>Total TDRs Outstanding</b>	<b>59</b>	<b>\$3,981,186</b>	<b>26</b>	<b>\$2,321,961</b>	<b>85</b>	<b>\$6,303,147</b>
<i>December 31, 2013</i>						
Member Business Loans:						
Not secured by real estate	1	\$ 170,000	-	\$ -	1	\$ 170,000
Member Consumer Loans:						
Not secured by real estate	34	205,857	8	76,024	42	281,881
<b>Total TDRs Outstanding</b>	<b>35</b>	<b>\$ 375,857</b>	<b>8</b>	<b>\$ 76,024</b>	<b>43</b>	<b>\$ 451,881</b>

**Hope Federal Credit Union**  
**Notes to Financial Statements**

**NOTE 4: LOANS RECEIVABLE (Continued)**

A summary of held for investment loans modified as TDRs that occurred during the year were as follows:

	2014			2013		
	Number	Pre-Modification Outstanding Balance	Post-Modification Outstanding Balance	Number	Pre-Modification Outstanding Balance	Post-Modification Outstanding Balance
<i>Years ended December 31,</i>						
Member Business Loans:						
Secured by real estate	2	\$ 1,097,131	\$ 1,097,131	3	\$ 184,563	\$ 181,950
Member Mortgage Loans	16	\$ 1,495,017	\$ 1,592,713	-	-	-
Member Consumer Loans:						
Secured by real estate	1	13,995	13,995	-	-	-
Not secured by real estate	5	73,959	72,047	11	81,149	79,615
<b>Total TDRs Outstanding</b>	<b>24</b>	<b>\$ 2,680,102</b>	<b>\$ 2,775,886</b>	<b>14</b>	<b>\$ 265,712</b>	<b>\$ 261,565</b>

***Allowance for Loan Losses***

Activity in the allowance for loan losses is as follows:

<i>December 31,</i>	2014	2013
Balance at beginning of year	\$ 1,618,971	\$ 1,626,099
Provisions for loan losses	901,688	827,602
Loans charged off	(1,016,482)	(1,441,519)
Recoveries	457,680	606,789
	<b>\$ 1,961,857</b>	<b>\$ 1,618,971</b>

Prior to 2014, Hope included an unallocated component to its allowance for loan losses to provide for credit losses incurred on originated mortgage loans prior to their sale. During 2014, Hope reclassified this portion of its allowance as an allocated component of the member mortgage loans which also includes a specific reserve for impaired loans.

## Hope Federal Credit Union Notes to Financial Statements

### NOTE 4: LOANS RECEIVABLE (Continued)

The balance in the allowance for possible loans losses by portfolio segment at December 31, 2014 and 2013 was as follows:

<i>December 31, 2014</i>	Balance at Beginning	Charge-Offs	Recoveries	Transfers	Provision for Loan Losses	Balances at End of Year
Member Business Loans:						
Real estate:						
Construction and land development	\$ 30,544	\$ -	\$ -	-	\$ 1,071	\$ 31,615
Single family	338,002	(113,160)	5,605	-	104,991	335,438
Commercial	139,454	(4,989)	584	-	2,687	137,736
Other	320,007	(41,360)	18,346	-	(3,737)	293,256
Commercial and industrial	137,141	(22,169)	6,059	-	153,269	274,300
Member Mortgage Loans	-	-	-	219,788	455,941	675,729
Member Consumer Loans:						
Secured by automobile loans	195,300	(346,499)	310,116	-	(122,735)	36,182
Unsecured loans	115,416	(386,279)	100,085	-	331,590	160,812
Secured by share accounts	2,368	(7,939)	617	-	12,864	7,910
Secured by real estate	-	(22,052)	15,261	-	13,288	6,497
Other secured consumer loans	53,138	(4,222)	1,007	-	(47,541)	2,382
Unallocated allowance	287,601	(67,813)	-	(219,788)	-	-
<b>Net Loans</b>	<b>\$ 1,618,971</b>	<b>\$ (1,016,482)</b>	<b>\$ 457,680</b>	<b>\$ -</b>	<b>\$ 901,688</b>	<b>\$ 1,961,857</b>

**Hope Federal Credit Union**  
**Notes to Financial Statements**

**NOTE 4: LOANS RECEIVABLE (Continued)**

<i>December 31, 2013</i>	Balance at Beginning of Year	Charge-Offs	Recoveries	Provision for Loan Losses	Balances at End of Year
Member Business Loans:					
Real estate:					
Construction and land development	\$ -	\$ -	\$ -	\$ 30,544	\$ 30,544
Single family	265,589	-	6,119	66,294	338,002
Commercial	189,736	(502,559)	-	452,277	139,454
Other	375,277	(447)	2,221	(57,044)	320,007
Commercial and industrial	121,687	-	-	15,454	137,141
Member Consumer Loans:					
Secured by automobile loans	289,331	(292,051)	400,339	(202,319)	195,300
Unsecured loans	72,582	(346,775)	133,156	256,453	115,416
Secured by share accounts	-	(2,857)	781	4,444	2,368
Secured by real estate	21,386	(8,153)	56,923	(70,156)	-
Other secured consumer loans	24,482	(58,594)	7,250	80,000	53,138
Unallocated allowance	266,029	(230,083)	-	251,655	287,601
<b>Net Loans</b>	<b>\$ 1,626,099</b>	<b>\$ (1,441,519)</b>	<b>\$ 606,789</b>	<b>\$ 827,602</b>	<b>\$ 1,618,971</b>

**NOTE 5: PREMISES AND EQUIPMENT**

Premises and equipment are as follows:

<i>December 31,</i>	<b>2014</b>	<b>2013</b>
Land	<b>\$ 976,450</b>	\$ 911,450
Buildings and improvements	<b>5,312,612</b>	4,808,968
Leasehold improvements	<b>115,551</b>	92,062
Computer and equipment	<b>2,861,926</b>	2,773,997
Furniture and fixtures	<b>936,418</b>	874,192
Construction in progress	-	1,869
	<b>\$ 10,202,957</b>	\$ 9,462,538
Less accumulated depreciation	<b>(3,911,087)</b>	(3,392,630)
	<b>\$ 6,291,870</b>	\$ 6,069,908

**Hope Federal Credit Union  
Notes to Financial Statements**

**NOTE 6: DEPOSITS AND MEMBERS' SHARE ACCOUNTS**

Deposits and members' share accounts are summarized as follows:

<i>December 31,</i>	<b>2014</b>	2013
Members' shares and clubs	<b>\$ 47,190,312</b>	\$ 56,147,768
Non-members' shares	<b>38,019</b>	98,912
Members' shares certificates	<b>64,255,847</b>	71,533,259
Non-members' certificates	<b>5,696,000</b>	409,703
Money market	<b>11,654,563</b>	12,523,058
	<b>\$ 128,834,741</b>	\$ 140,712,700

Included in members' share accounts and certificates were member certificates in amounts of \$100,000 or more. These certificates approximated \$78,722,000 and \$89,795,000 at December 31, 2014 and 2013, respectively.

Interest expense on members' share and deposit accounts is summarized as follows:

<i>Years ended December 31,</i>	<b>2014</b>	2013
Share certificates and clubs	<b>\$ 898,847</b>	\$ 1,049,203
Money market and savings	<b>193,974</b>	251,045
	<b>\$ 1,092,821</b>	\$ 1,300,248

A summary of maturities of member and non-member share certificates at December 31, 2014 are as follows:

Maturity within one year	<b>\$ 30,086,452</b>
Maturity one to five years	<b>39,852,983</b>
Maturity more than five years	<b>12,412</b>
	<b>\$ 69,951,847</b>

***Related Party Deposits***

In the ordinary course of business, officers and upper management have deposit accounts with Hope. The deposit accounts totaled approximated \$700,000 at December 31, 2014 and \$148,000 at December 31, 2013. Management believes these deposit accounts had the same terms, including interest rates, as those prevailing at the time for comparable transactions with other persons.

## Hope Federal Credit Union Notes to Financial Statements

### NOTE 7: LINE OF CREDIT

Hope has entered into a loan agreement with a financial institution which provides for borrowings up to \$12,000,000 as of December 31, 2014 and 2013 under a line of credit arrangement. Advances under the lines of credit are repayable within thirty days from the date of each advance. As of December 31, 2014, Hope had borrowings outstanding of \$2,000,000 secured by qualifying investments held for sale with an estimated fair value equal to 120% of amounts outstanding and which matures on January 12, 2015. The short term borrowing bears interest based the federal funds rate plus 200 basis points (effective rate of 2.25% as of December 31, 2014). There were no amounts outstanding under this borrowing arrangement as of December 31, 2013. Pursuant to the loan agreement, the revolving line of credit expires on May 6, 2015.

### NOTE 8: FEDERAL HOME LOAN BANK ADVANCES

Hope is a member of the Federal Home Loan Bank of Dallas ("FHLB") and has entered into credit arrangements with the FHLB under which authorized borrowings are collateralized by Hope's FHLB stock as well as loans or other instruments which may be pledged. These advances carry a fixed rate of interest and approximated \$24,205,000 and \$21,702,000 at December 31, 2014 and 2013, respectively. Hope has pledged a security interest in its real estate loan portfolio to the FHLB as collateral for these borrowings with a carrying value of approximately \$33,302,000 and \$32,556,000 as of December 31, 2014 and 2013, respectively. In addition, short term investments with a carrying value of approximately \$1,156,000 are pledged as collateral for the FHLB advances.

A summary of the FHLB borrowings at December 31, 2014 and 2013 were as follows:

Maturity Year	Interest Rate Range	2014	2013
Maturing in 2014	0.450%	\$ -	\$ 250,000
Maturing in 2015	0.450% - 0.940%	3,500,000	3,500,000
Maturing in 2017	0.90% - 0.95%	750,000	750,000
Maturing in 2018	0.900%	250,000	250,000
Maturing in 2018	4.014% - 4.148%	2,557,873	3,135,909
Maturing in 2019	1.600%	250,000	250,000
Maturing in 2020	1.500%	250,000	250,000
Maturing in 2021	2.187% - 2.278%	2,344,902	2,651,994
Maturing in 2022	1.790% - 2.283%	3,885,599	4,215,421
Maturing in 2023	1.829% - 2.100%	1,933,636	2,119,979
Maturing in 2024	2.350% - 2.441%	1,925,641	-
Maturing in 2025	2.217%	2,500,000	-
Maturing in 2027	2.365% - 2.753%	2,965,996	3,168,849
Maturing in 2028	2.174%	1,090,985	1,160,273
		<b>\$ 24,204,632</b>	<b>\$ 21,702,425</b>

**Hope Federal Credit Union  
Notes to Financial Statements**

**NOTE 8: FEDERAL HOME LOAN BANK ADVANCES (Continued)**

A summary of the maturity of FHLB borrowings by year over the next five years and amounts maturing thereafter as of December 31, 2014 are as follows:

2015	\$	3,500,000
2016		-
2017		750,000
2018		2,807,873
2019		250,000
Maturing thereafter		16,896,759
		\$ 24,204,632

**NOTE 9: SECONDARY CAPITAL LOANS**

Secondary capital loans consist of funding from private sources or affiliates of Hope’s primary sponsor and from senior subordinated debentures issued pursuant to the Community Development Capital Initiative (“CDCI”) program established by the U. S. Treasury for financial institutions that have been certified as community development financial institutions (“CDFI”).

To be certified as a CDFI, a financial institution must demonstrate that it serves an eligible target market and that at least 60% of its activities are directed to that target market. As a qualifying CDFI, Hope was eligible to apply for a CDCI capital investment of up to 3.5% of its total assets and no more than 50% of its capital and surplus. In connection therewith, Hope received the CDCI funding through the issuance of senior subordinated debentures qualifying as secondary capital loans totaling \$4,520,000.

These secondary capital loans are available to cover any and all quarterly operating losses that exceed Hope's net available reserves and undivided earnings. Secondary capital loans used to cover operating losses are not required to be repaid and are recognized as income in the period the losses are incurred.

The variable rate secondary capital loans require principal repayments, unless Hope (i) would be unable to fully service existing senior indebtedness, (ii) would be unable to satisfy its operating expenses, or (iii) would not have available cash flows for the withdrawal of funds for the account.

The senior subordinated debentures have a maturity of 13 years and bear interest at 2% per annum until the 8<sup>th</sup> anniversary of the closing date (September 17, 2010) and thereafter at a rate of 9% per annum. The debentures are subordinated to claims of creditors, shareholders (depositors) and the National Credit Union Share Insurance Fund and may be redeemed prior to maturity at Hope’s option, subject to approval by its regulatory authority. The debentures were issued pursuant to a securities purchase agreement which contains covenants that require continued eligibility and compliance with CDFI requirements and place limitations on the amount of executive compensation and dividends and repurchases of equity and debt instruments.

**Hope Federal Credit Union**  
**Notes to Financial Statements**

**NOTE 9: SECONDARY CAPITAL LOANS (Continued)**

Holders of the senior subordinated debentures have no voting rights, except under certain circumstances, including amendments to the senior subordinated securities and certain merger, exchange or consolidation events.

Secondary capital loans consisted of the following:

<i>December 31,</i>	<b>2014</b>	<b>2013</b>
Fixed rate loan from Hope Enterprise Corporation bearing interest at 1.00% per annum, maturing on December 31, 2019	<b>\$ 5,000,000</b>	\$ 5,000,000
Senior subordinated debenture payable to the U. S. Treasury maturing on September 17, 2023 and bearing interest at 2% through September 17, 2018 and 9% per annum thereafter	<b>4,520,000</b>	4,520,000
Fixed rate loan from ECD New Markets, LLC bearing interest at 5.45% per annum, maturing on January 1, 2027 and with quarterly principal repayments of \$250,000 beginning January 1, 2015	<b>4,050,000</b>	4,050,000
Variable rate loan from ECD New Markets, LLC bearing interest at a minimum rate of 5% and a maximum rate of 10% (effective rate of 5.00% at December 31, 2014 and 2013, maturing on June 22, 2025 and with an annual principal payment due on June 22, 2015 of \$1,852,000	<b>2,677,500</b>	3,060,000
Variable rate loan from ECD New Markets, LLC bearing interest at a minimum rate of 5.45% and a maximum rate of 10.9% (effective rate of 5.45% at December 31, 2014 and 2013), maturing on September 28, 2024	<b>550,000</b>	1,548,000
Variable rate loan from ECD New Markets, LLC bearing interest at a minimum rate of 5% and a maximum rate of 10% (effective rate of 5% at December 31, 2014 and 2013), maturing on December 20, 2024	<b>550,000</b>	1,548,000
Zero interest loan from a bank due on demand	<b>76,724</b>	76,724
	<b>17,424,224</b>	19,802,724
Less maturity reclassification	<b>(4,329,224)</b>	(5,737,224)
	<b>\$ 13,095,000</b>	\$ 14,065,500

As a low-income designated credit union, Hope is allowed to offer secondary capital loans which are considered a component of net worth for regulatory purposes until they reach a maturity of five years or less. Secondary capital loans with maturities of five years or less are reclassified as

## Hope Federal Credit Union Notes to Financial Statements

### NOTE 9: SECONDARY CAPITAL LOANS (Continued)

subordinated debt, through a maturity reclassification adjustment of one-fifth of the amount due within five years. As of December 31, 2014 and 2013, approximately \$4,329,000 and \$5,737,000, respectively, were reclassified under these regulatory requirements.

A summary of the maturity reclassifications of secondary capital loans by year over the next five years and amounts maturing thereafter as of December 31, 2014 are as follows:

2015	\$ 2,929,224
2016	1,000,000
2017	1,000,000
2018	-
2019	5,000,000
Maturing thereafter	7,495,000
	\$ 17,424,224

### NOTE 10: MEMBERS' EQUITY

Hope 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 Hope's financial statements. Under capital adequacy regulations and the regulatory framework for prompt corrective action, a 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 regulatory accounting practices. Hope's capital amounts and net worth classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require a credit union to maintain minimum amounts and ratios (set forth in the table below) of net worth to total assets, as defined. Credit unions are also required to calculate a risk-based net worth (RBNW) requirement which establishes whether or not the credit union will be considered complex under the regulatory framework. Hope's net worth ratio as of December 31, 2014 and 2013 was 9.79% and 8.93%, respectively. The minimum ratio to be considered complex under the regulatory framework is 6 percent. Management believes, as of December 31, 2014, that Hope meets all capital adequacy requirements to which it is subject.

As of December 31, 2014, the most recent call reporting period, Hope was categorized as "*well capitalized*" under the NCUA regulatory framework for prompt corrective action. To be categorized as "*well capitalized*" a credit union must maintain a minimum net worth ratio of 7 percent of assets and meet any applicable risk-based net worth requirements.

## Hope Federal Credit Union Notes to Financial Statements

### NOTE 10: MEMBERS' EQUITY (Continued)

Hope's actual regulatory capital amounts and ratios as of December 31, 2014 and 2013 (using quarter end balances, as permitted by regulation) are presented below:

	Actual		For Capital Adequacy Purposed:		To Be Well Capitalized Under Prompt Corrective Action Provisions:	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
<b>At December 31, 2014</b>						
Regulatory Net Worth	\$ 17,478,506	9.79%	10,707,170	6.00%	12,491,698	7.00%
Risk-Based Net Worth Requirements	\$ 10,992,695	6.16%	N/A	N/A	N/A	N/A
<b>At December 31, 2013</b>						
Regulatory Net Worth	\$ 16,664,034	8.93%	11,202,985	6.00%	13,070,117	7.00%
Risk-Based Net Worth Requirements	\$ 10,232,035	5.48%	N/A	N/A	N/A	N/A

Hope is also subject to various U. S. Department of Housing and Urban Development (HUD) regulatory guidelines including minimum capital requirements in connection with seller-servicer agreements that Hope has entered into with secondary market investors. Failure to maintain minimum capital requirements could result in Hope's inability to originate and sell loans for the respective investor and, therefore, could have a direct material effect on Hope's financial statements. As of December 31, 2014 and 2013, Hope was in compliance with HUD guidelines and the various capital requirements by secondary market investors.

### NOTE 11: ACTIVITIES WITH PRIMARY SPONSOR

Hope Enterprise Corporation (HEC) is the primary sponsoring organization of Hope and operates as a community development financial institution for the purpose of providing investment capital to rural and economically disadvantaged communities. As part of its strategy, HEC and certain of its affiliates have provided grants and secondary capital loans to Hope in order to provide an affordable lending program to low-income communities. Further, Hope and HEC have entered into certain contractual arrangements wherein HEC agreed to reimburse Hope for certain operating expenses and for certain losses incurred on loans considered to be higher risk than typically underwritten by regulated financial institutions. Under the terms of the contractual arrangements, Hope has agreed to provide financial products and service offerings in certain low-income communities in which HEC has a mission to promote economic development. In consideration for these contractual services, HEC has agreed to reimburse Hope for its normal operating expenses, excluding dividend payments, on a monthly basis. The contractual arrangements provide for a limitation on the fluctuating monthly amount HEC will reimburse Hope which is based upon a maximum monthly net income level of \$20,000.

**NOTE 11: ACTIVITIES WITH PRIMARY SPONSOR (Continued)**

During 2014 and 2013, Hope recognized contractual service revenue of approximately \$0 and \$700,000, respectively, relative to these arrangements. In addition, Hope received grants from third parties of approximately \$1,049,000 in 2014 and \$1,506,000 in 2013 that were passed to Hope from HEC and its affiliates.

As of December 31, 2014 and 2013, Hope had secondary capital loans outstanding to HEC and its affiliates of approximately \$12,828,000 and \$15,206,000, respectively. Interest expense relating to these affiliated secondary capital loans approximated \$560,000 in 2014 and \$626,000 in 2013.

As of December 31, 2014 and 2013, HEC had deposit accounts with Hope totaling approximately \$5,256,000 and \$5,151,000, respectively.

As of December 31, 2014 and 2013, Hope had a real estate secured loan receivable outstanding from HEC of approximately \$1,044,000 and \$1,087,000, respectively. The real estate loan receivable is repayable in monthly installments of \$7,773, including interest at prime plus 1.5%, and with a final balloon payment in December 2020. In addition, Hope has a loan receivable from HEC for working capital of approximately \$89,000 and \$152,000 as of December 31, 2014 and 2013, respectively, which bears interest at 6% and is repayable in monthly installments of \$5,849 through May 2016. Interest income recognized on these related party loans approximate \$58,000 and \$62,000 in 2014 and 2013, respectively.

Accounts payable to HEC approximated \$23,000 as of December 31, 2014 and represented amounts due for certain loan fees owed to HEC. Accounts receivable from HEC approximated \$641,000 as of December 31, 2013, and represented amounts due for unconditional grant pledges and contractual services.

Annually HEC incurs certain other expenses on behalf of Hope that are not reflected in the accompanying financial statements. These expenses include cost for certain personnel resources, marketing efforts and executing capital campaign strategies to support Hope's operations.

**NOTE 12: FAIR VALUE MEASUREMENTS**

Investment securities available for sale were measured at fair value using level 2 inputs and represent the only financial assets measured at fair value by Hope on a recurring basis at December 31, 2014 and 2013.

Certain financial assets and financial liabilities are measured at fair value on a nonrecurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). Hope has no financial liabilities measured at fair value on a non-recurring basis.

**NOTE 12: FAIR VALUE MEASUREMENTS (Continued)**

Financial assets of Hope measured at fair value at year end on a non-recurring basis include certain impaired loans reported at the fair value of the underlying collateral if repayment is expected solely from the collateral. The impaired loans are reported at fair value through a specific valuation allowance allocation of the allowance for possible loan losses. Collateral values are estimated using Level 2 inputs based on observable market data or Level 3 inputs based on customized discounting criteria. As of December 31, 2014, impaired loans with a carrying value of \$3,330,000 were reduced by specific valuation allowance allocations totaling \$546,000 to a total reported fair value of \$2,784,000 based on collateral valuations utilizing Level 3 valuation inputs. As of December 31, 2013, impaired loans with a carrying value of \$1,358,000 were reduced by specific valuation allowance allocations totaling \$97,000 to a total reported fair value of \$1,261,000 based on collateral valuations utilizing Level 3 valuation inputs.

Hope has no non-financial assets or non-financial liabilities measured at fair value on a recurring basis. Certain non-financial assets and non-financial liabilities measured at fair value on a non-recurring basis include foreclosed assets (upon initial recognition or subsequent impairment) and non-financial assets measured at fair value in the second step of a goodwill impairment test.

During 2014 and 2013, certain foreclosed assets, upon initial recognition, were measured and reported at fair value through a charge-off to the allowance for possible loan losses based upon the fair value of the foreclosed asset. The fair value of a foreclosed asset, upon initial recognition, is estimated using Level 2 inputs based on observable market data or Level 3 inputs based on customized discounting criteria. Foreclosed assets measured at fair value upon initial recognition totaled \$491,000 and \$746,000 (utilizing Level 3 valuation inputs) during 2014 and 2013, respectively. In connection with the measurement and initial recognition of the aforementioned foreclosed assets, Hope recognized charge-offs to the allowance for loan losses of approximately \$100,000 during 2014 and \$276,000 during 2013. Additionally, Hope recognized impairment losses of approximately \$7,000 in 2014 and \$108,000 in 2013 as a result of subsequent fair value remeasurements relating to foreclosed property held utilizing Level 3 valuation inputs.

Appraisals are generally obtained and used for impaired loan and foreclosed real estate valuation assessments. These appraisals incorporate measures such as recent sales prices for comparable properties or customized discounting criteria. Accordingly, collateral values are generally estimated using Level 3 valuation inputs.

Mortgage loans held-for-sale are carried at the lower of cost or fair value. The fair value of loans held-for-sale is based on discounted cash flows using prices currently being offered for portfolios with similar characteristics in the secondary markets. At December 31, 2014 and 2013, the aggregate carrying value of Hope's mortgage loans held-for-sale was less than the estimated fair value.

## Hope Federal Credit Union Notes to Financial Statements

### NOTE 13: DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying values and estimated fair values of Hope's financial instruments at December 31, 2014 and 2013 were as follows:

	2014		2013	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
<b>Financial Assets:</b>				
Cash and cash equivalents	\$ 19,527,081	\$ 19,527,081	\$ 35,850,309	\$ 35,850,309
Short-term investments	1,387,196	1,387,196	2,023,857	2,023,857
Investment securities available for sale	17,689,003	17,689,003	16,389,729	16,389,729
Mortgage loans held for sale	-	-	57,756,017	62,995,545
Loans receivable	127,020,959	131,506,778	60,856,368	61,291,344
Restricted investment securities	1,068,000	1,068,000	995,900	995,900
NCUSIF deposits	1,190,154	1,190,154	1,172,728	1,172,728
<b>Financial Liabilities:</b>				
Deposits and members' share accounts	128,834,741	129,209,650	140,712,700	141,075,672
Short-term borrowings	2,000,000	2,000,000	-	-
Federal Home Loan Bank advances	24,204,632	24,247,544	21,702,425	22,645,285
Secondary capital loans	17,424,224	18,882,044	19,802,724	20,663,052

Certain other financial instruments are not carried at fair value in the accompanying statements of financial condition, including accounts receivable, accrued interest receivable and payable, accounts payable and accrued liabilities. The carrying amount of these financial instruments not carried at fair value is a reasonable estimate of fair value because of the generally short periods of time in which related assets or liabilities are expected to be realized or liquidated, and because they do not present unanticipated credit concern.

The estimated fair values are significantly affected by assumptions used, principally the timing of future cash flows, the discount rate, judgments regarding current economic conditions, risk characteristics of various financial instruments and other factors. Because assumptions are inherently subjective in nature, the estimated fair values cannot be substantiated by comparison to independent quotes, and in many cases, the estimated fair values could not necessarily be realized in an immediate sale or settlement of the instrument. Potential tax ramifications related to the realization of unrealized gains and losses that would be incurred in an actual sale and/or settlement have not been taken into consideration.

**NOTE 14: COMMITMENTS AND CONTINGENCIES**

***Interest Rate Risk***

Hope provides short-term and medium-term commercial and consumer loans with interest rates that are fixed or fluctuate with the prime lending rate. These loans are primarily funded through short-term member share accounts and certificates or secondary capital loans with variable and fixed rates. Accordingly, Hope is exposed to interest rate risk because, in changing interest rate environments, interest rate adjustments on assets and liabilities may not occur at the same time or in the same amount. Hope manages the overall rate sensitivity and mix of its asset and liability portfolio and attempts to minimize the effects that interest rate fluctuations will have on its net interest margin.

Hope is a party to various financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its members. These financial instruments include commitments to extend credit and originate mortgage loans. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the financial statements. The contract or notional amounts of those instruments reflect the extent of the involvement Hope has in particular classes of financial instruments. Since some of these commitments are expected to expire without being drawn upon, the total commitment amount does not necessarily represent future cash requirements.

Hope's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit is represented by the contractual notional amount of those instruments. Hope uses the same credit policies in making these commitments and conditional obligations as it does for on-balance sheet instruments.

As of December 31, 2014 and 2013, Hope had commitments to extend credit of approximately \$20,198,000 and \$11,140,000, respectively, based upon the contractual amount of the commitment to the respective member borrower.

***Concentration of Credit Risk***

At December 31, 2014, Hope had cash deposits with four financial institutions, including their central clearing house, in excess of insured limits by approximately \$10,657,000. Hope periodically assesses the financial condition of these financial institutions and believes the risk of any loss is minimal.

Hope makes loans to individuals and small businesses located in rural, economically disadvantaged areas of Mississippi, Louisiana, Tennessee and Arkansas. Such loans, the proceeds of which normally provide consumer financing to individuals and working capital, equipment, and facilities financing to undercapitalized businesses that may be unable to obtain credit from conventional financing sources, carry a higher than typical degree of risk.

**NOTE 14: COMMITMENTS AND CONTINGENCIES (Continued)**

***Litigation***

Hope is defendant in litigation arising during normal business activities. Management, with the advice of legal counsel, is of the opinion that the ultimate resolution of these matters will not have a material adverse effect on the financial statements.