

**ORANGE COUNTY'S CREDIT UNION  
AND SUBSIDIARY  
Santa Ana, California**

**CONSOLIDATED FINANCIAL STATEMENTS  
December 31, 2009 and 2008**

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## Independent Auditor's Report

Members of the Supervisory Committee and  
Board of Directors  
Orange County's Credit Union and subsidiary  
Santa Ana, California

We have audited the accompanying consolidated statements of financial condition of Orange County's Credit Union and subsidiary as of December 31, 2009 and 2008, and the related consolidated statements of operations, members' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Credit Union's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Orange County's Credit Union and subsidiary as of December 31, 2009 and 2008, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

*Clifton Gunderson LLP*

Tucson, Arizona  
April 7, 2010

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY**  
**CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION**  
**December 31, 2009 and 2008**

<b>ASSETS</b>		
	<u><b>2009</b></u>	<u><b>2008</b></u>
Cash and cash equivalents	\$ 89,656,852	\$ 65,977,711
Investment securities:		
Available-for-sale	47,303,252	26,382,624
Other investments	185,525,145	104,950,234
Federal Home Loan Bank stock	3,550,900	3,219,600
Loans held-for-sale	5,248,538	981,000
Loans to members, net of allowance for loan losses	554,847,466	653,375,531
Accrued interest receivable	2,604,946	3,137,933
Premises and equipment, net	23,269,127	24,431,017
NCUSIF deposit	8,075,425	7,251,153
Foreclosed assets	725,775	1,139,195
Other assets	<u>3,247,803</u>	<u>2,586,455</u>
 <b>TOTAL ASSETS</b>	 <u><b>\$ 924,055,229</b></u>	 <u><b>\$ 893,432,453</b></u>
 <b>LIABILITIES AND MEMBERS' EQUITY</b>		
<b>LIABILITIES</b>		
Members' share and savings accounts	\$ 829,930,035	\$ 796,307,276
Borrowed funds	13,100,000	14,350,000
Accrued expenses and other liabilities	<u>2,364,005</u>	<u>3,450,011</u>
 Total liabilities	 <u>845,394,040</u>	 <u>814,107,287</u>
 <b>MEMBERS' EQUITY - substantially restricted</b>		
Regular reserve	14,248,147	14,248,147
Undivided earnings	64,359,649	64,785,427
Accumulated other comprehensive income	<u>53,393</u>	<u>291,592</u>
 Total members' equity	 <u>78,661,189</u>	 <u>79,325,166</u>
 <b>TOTAL LIABILITIES AND MEMBERS' EQUITY</b>	 <u><b>\$ 924,055,229</b></u>	 <u><b>\$ 893,432,453</b></u>

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

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF OPERATIONS  
Years Ended December 31, 2009 and 2008**

	<u>2009</u>	<u>2008</u>
<b>INTEREST INCOME</b>		
Interest on loans to members	\$ 38,861,707	\$ 42,349,213
Interest on investment securities and cash equivalents	<u>5,303,627</u>	<u>7,342,723</u>
Total interest income	<u>44,165,334</u>	<u>49,691,936</u>
<b>INTEREST EXPENSE</b>		
Dividends on members' share and savings accounts	12,151,522	20,647,451
Interest on borrowed funds	<u>524,210</u>	<u>420,763</u>
Total interest expense	<u>12,675,732</u>	<u>21,068,214</u>
Net interest income	31,489,602	28,623,722
<b>PROVISION FOR LOAN LOSSES</b>	<u>11,471,792</u>	<u>13,078,520</u>
Net interest income after provision for loan losses	<u>20,017,810</u>	<u>15,545,202</u>
<b>NON-INTEREST INCOME</b>		
Fees and charges	6,120,165	6,106,485
Other non-interest income	5,728,674	5,717,506
Gain on sales of loans held-for-sale	<u>521,526</u>	<u>42,272</u>
Total non-interest income	<u>12,370,365</u>	<u>11,866,263</u>
<b>NON-INTEREST EXPENSE</b>		
Compensation and benefits	17,010,092	17,186,870
Occupancy	2,632,425	2,661,760
Operations	7,074,699	7,680,897
NCUSIF premium assessment	1,211,314	-
Professional and outside services	601,114	910,944
Educational and promotional	489,428	881,590
Loan servicing	1,171,014	797,497
Impairment loss on Members United capital account	1,053,294	-
Impairment loss on Southwest Corporate capital account	726,795	-
Impairment loss on WesCorp capital accounts	-	8,785,196
Other expense	<u>843,778</u>	<u>1,346,131</u>
Total non-interest expense	<u>32,813,953</u>	<u>40,250,885</u>
<b>NET LOSS</b>	<u>\$ (425,778)</u>	<u>\$ (12,839,420)</u>

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

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF MEMBERS' EQUITY  
Years Ended December 31, 2009 and 2008**

	Regular Reserve	Undivided Earnings	Accumulated Other Comprehensive Income (Loss)	Total
<b>BALANCES, DECEMBER 31, 2007</b>	\$ 14,248,147	\$ 77,624,847	\$ 115,160	\$ 91,988,154
<b>COMPREHENSIVE LOSS</b>				
Net loss	-	(12,839,420)	-	(12,839,420)
Other comprehensive income:				
Change in unrealized gain (loss) on securities available-for-sale	-	-	176,432	176,432
Total comprehensive loss				(12,662,988)
<b>BALANCES, DECEMBER 31, 2008</b>	14,248,147	64,785,427	291,592	79,325,166
<b>COMPREHENSIVE LOSS</b>				
Net loss	-	(425,778)	-	(425,778)
Other comprehensive loss:				
Change in unrealized gain (loss) on securities available-for-sale	-	-	(238,199)	(238,199)
Total comprehensive loss				(663,977)
<b>BALANCES, DECEMBER 31, 2009</b>	\$ 14,248,147	\$ 64,359,649	\$ 53,393	\$ 78,661,189

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

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**Years Ended December 31, 2009 and 2008**

	<u>2009</u>	<u>2008</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net loss	\$ (425,778)	\$ (12,839,420)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	1,746,348	1,693,843
Amortization of premiums and discounts, net	72,728	47,113
Amortization of deferred loan origination fees and costs, net	(285,684)	132,980
Provision for loan losses	11,471,792	13,078,520
Impairment loss on Members United capital account	1,053,294	-
Impairment loss on Southwest Corporate capital account	726,795	-
Impairment loss on WesCorp capital accounts	-	8,785,196
Loss on foreclosed assets	48,494	40,836
Effect of changes in operating assets and liabilities:		
Loans held-for-sale	(4,267,538)	(892,699)
Accrued interest receivable	532,987	72,924
Other assets	(661,348)	488,039
Accrued expenses and other liabilities	<u>(1,086,006)</u>	<u>(871,126)</u>
Net cash provided by operating activities	<u>8,926,084</u>	<u>9,736,206</u>
 <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Proceeds from repayments or maturity of available-for-sale securities	22,350,820	17,693,481
Purchases of available-for-sale securities	(43,582,375)	(9,500,000)
Proceeds from repayments or maturity of held-to-maturity securities	-	1,000,000
Increase in deposits in corporate credit union accounts	(82,255,000)	(21,890,399)
Net increase in other investments	(100,000)	-
Increase in Federal Home Loan Bank stock	(331,300)	(294,900)
Loans to members, net of principal collections	86,135,741	(25,059,370)
Increase in NCUSIF deposit	(824,272)	(922,275)
Deferred compensation distribution	-	(1,058,997)
Purchases of premises and equipment	(584,458)	(1,770,571)
Proceeds from sale of foreclosed assets	<u>1,571,142</u>	<u>-</u>
Net cash used in investing activities	<u>(17,619,702)</u>	<u>(41,803,031)</u>
 <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Net increase in members' share and savings accounts	33,622,759	39,892,465
Proceeds received on borrowed funds	-	9,000,000
Payments made on borrowed funds	<u>(1,250,000)</u>	<u>(2,500,000)</u>
Net cash provided by financing activities	<u>32,372,759</u>	<u>46,392,465</u>

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)**  
**Years Ended December 31, 2009 and 2008**

	<u>2009</u>	<u>2008</u>
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	\$ 23,679,141	\$ 14,325,640
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR</b>	<u>65,977,711</u>	<u>51,652,071</u>
<b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>	<u>\$ 89,656,852</u>	<u>\$ 65,977,711</u>
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>		
Cash paid during the year for interest:		
Dividends on members' share and savings accounts	\$ 12,151,522	\$ 20,647,451
Interest on borrowed funds	<u>524,210</u>	<u>420,763</u>
Total	<u>\$ 12,675,732</u>	<u>\$ 21,068,214</u>
Taxes paid	<u>\$ 50,089</u>	<u>\$ 118,015</u>
Transfers from loans to foreclosed assets	<u>\$ 1,206,216</u>	<u>\$ 1,180,031</u>

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

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
December 31, 2009 and 2008**

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Nature of Operations**

Orange County's Credit Union is a state chartered credit union organized under the provisions of the California Credit Union Act and administratively responsible to the California Department of Financial Institutions. The primary purpose is to promote thrift among, and create a source of credit for its members. Participation in the Credit Union is limited to those individuals that qualify for membership. The field of membership is defined in the Credit Union's Charter and Bylaws. The Credit Union's primary source of revenue is providing loans to its members. The CUSO is engaged in providing insurance products to members.

**Principles of Consolidation**

The consolidated financial statements include the accounts of Orange County's Credit Union (Credit Union) and its wholly owned subsidiary, Orange County Group, Inc. (CUSO). No significant net income is derived from the CUSO. All significant intercompany accounts and transactions have been eliminated.

**Use of Estimates in Preparing Consolidated Financial Statements**

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

**Significant Group Concentrations of Credit Risk**

The Credit Union provides a variety of financial services to its members, most of who live, work, or worship in Orange County, California and Riverside County, California. The Credit Union may be exposed to credit risk from a regional economic standpoint because of significant concentration of its borrowers work or reside in the state of California. However, the loan portfolio is well diversified and the Credit Union does not have any significant concentrations of credit risk except for real estate, automobile and member business loans. The Credit Union's policy for repossessing collateral is that when all other collection efforts have been exhausted, the Credit Union enforces its first lien holder status and repossesses the collateral. The Credit Union has full and complete access to repossessed collateral. Repossessed collateral normally consists of vehicles and residential and commercial real estate.

**Cash and Cash Equivalents**

For purposes of the consolidated statements of financial condition and the consolidated statements of cash flows, cash and cash equivalents includes cash on hand, amounts due from financial institutions, and highly liquid debt instruments with original maturities of three months or less. Amounts due from financial institutions may, at times, exceed federally insured limits.

**Investment Securities**

Debt and equity securities that management has the positive intent and ability to hold to maturity are classified as "held-to-maturity" and recorded at amortized cost, adjusted for amortization of premiums and accretion of discounts. Securities not classified as held-to-maturity or trading, including debt and equity securities with readily determinable fair values, are classified as "available-for-sale" and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income.

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
December 31, 2009 and 2008**

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Investment Securities** (Continued)

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Credit Union to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in its fair value. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method. The Credit Union does not maintain a trading or held-to-maturity portfolio. Other investments are classified separately and are stated at cost.

**Federal Home Loan Bank Stock**

The Credit Union, as a member of the Federal Home Loan Bank (FHLB) system, is required to maintain an investment in capital stock of the FHLB in an amount equal to the greater of 1% of its membership assets or 4.7% of advances from the FHLB. There is no ready market value for the FHLB stock; therefore, it has no quoted market value and is reported on the consolidated statement of financial position at cost.

**Loans Held-For-Sale**

Loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value in the aggregate, as determined by aggregate outstanding commitments from investors or current investor yield requirements. Net unrealized losses are recognized through a valuation allowance by charges to income. All sales are made without recourse.

**Loans to Members**

The Credit Union grants mortgage, member business and consumer loans to members. A substantial portion of the loan portfolio is represented by automobile and real estate loans to members. A substantial portion of its members' ability to honor their loan agreements is dependent upon the economic stability of the various groups comprising the Credit Union's field of membership.

Loans that the Credit Union has the intent and ability to hold for the foreseeable future are stated at unpaid principal balances, less an allowance for loan losses and net deferred loan origination costs. Interest on loans is recognized over the term of the loan and is generally calculated using the simple-interest method on principal amounts outstanding.

The accrual of interest on loans is discontinued at the time a loan is 60 days delinquent. Consumer loans are typically charged-off no later than 180 days past due. Loans may be charged-off at an earlier date if collection of principal or interest is considered doubtful. Past due loan status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged-off at an earlier date if management believes, after considering economic conditions, business conditions, and collection efforts, that collection of principal or interest is considered doubtful.

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
December 31, 2009 and 2008**

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Loans to Members** (Continued)

All interest accrued but not collected for loans that are placed on nonaccrual or charged-off is reversed against interest income. The interest on these loans is accounted for on the cash-basis method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Certain direct loan origination costs are deferred, and the net fee or cost is recognized as an adjustment to interest income using the interest method (first mortgage loans) and the effective yield method, which approximates the interest method (all other loan types) over the contractual life of the loans, adjusted for estimated prepayments based on the Credit Union's historical prepayment experience.

**Allowance for Loan Losses**

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

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

The Credit Union's allowance for loan losses is that amount considered adequate to absorb probable losses in the portfolio based on management's evaluations of the size and current risk characteristics of the loan portfolio. Such evaluations consider prior loss experience, the risk rating distribution of the portfolios, the impact of current internal and external influences on credit loss and the levels of nonperforming loans. General allowances are established for loans that can be grouped into pools based on similar characteristics as described in ASC 310-10-35 (SFAS No. 5 *Accounting for Contingencies*). In this process, general allowance factors are based on an analysis of historical charge-off experience and expected losses given default derived from the Credit Union's internal risk rating process. These factors are developed and applied to the portfolio in terms of loan type. The qualitative factors associated with the allowances are subjective and require a high degree of management judgment. Specific allowances for loan losses are established for large non-homogeneous impaired loans on an individual basis as required per ASC 310-10-35 (SFAS No. 114, *Accounting by Creditors for Impairment of a Loan*). The specific allowance established for these loans is based on a thorough analysis of the most probable source of repayment, including the present value of the loan's expected future cash flow, the loan's estimated market value, or the estimated fair value of the underlying collateral. These factors include the credit quality statistics, recent economic uncertainty, losses incurred from recent events, and lagging data.

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
December 31, 2009 and 2008**

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Allowance for Loan Losses (Continued)**

A loan is considered impaired when, based on current information and events, it is probable that the Credit Union will be unable to collect the scheduled payments of principal 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 that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for member business and residential real estate loans by either the present value of the expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Credit Union does not separately identify individual consumer loans for impairment disclosures.

**Off-Balance Sheet Credit Related Financial Instruments**

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

**Foreclosed Assets**

Assets acquired through, or in lieu of, loan foreclosures are held for sale and are initially recorded at fair value at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less costs to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net expenses from foreclosed assets.

**Transfers of Financial Assets**

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

**Premises and Equipment**

Land is carried at cost. Buildings and improvements, furniture and equipment and leasehold improvements are carried at cost, less accumulated depreciation and amortization. Buildings and improvements and furniture and equipment are depreciated using the straight-line method over the estimated useful lives of the assets. The cost of leasehold improvements is amortized using the straight-line method over the terms of the related leases.

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
December 31, 2009 and 2008**

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Valuation of Long-Lived Assets**

The Credit Union accounts for the valuation of long-lived assets under ASC 360-10-35 (SFAS No. 144, *Accounting for Impairment or Disposal of Long-Lived Assets*). This standard requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Management reviews all material assets annually for possible impairment. If such assets are considered to be impaired, the impairment recognized is measured as the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets.

**NCUSIF 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 would be refunded to the Credit Union if its insurance coverage is terminated, it converts to insurance coverage from another source, or the operations of the fund are transferred from the NCUA Board.

**NCUSIF Insurance Premiums**

A credit union is required to pay an annual insurance premium equal to one-twelfth of 1 percent of its total insured shares, unless the payment is waived or reduced by the NCUA Board.

**Members' Share and Savings Accounts**

Members' share and savings accounts are subordinated to all other liabilities of the Credit Union upon liquidation. Interest on members' share and savings accounts are based on available earnings at the end of a dividend period and are not guaranteed by the Credit Union. Interest rates on members' share and savings accounts are set by Management, based on an evaluation of current and future market conditions.

**Members' Equity**

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

**Income Taxes**

The Credit Union is exempt, by statute, from federal and state income taxes. The CUSO, however, is subject to federal and state income taxes. Operations of the CUSO resulted in income tax expense of \$30,088 and \$102,773 for the years ended December 31, 2009 and 2008, respectively.

The Credit Union is a tax-exempt entity under Internal Revenue Code 501(c)(14), but may be subject to taxation on income unrelated to the Credit Union's exempt function. In 2007, the Internal Revenue Service (IRS) issued 25 Technical Advice Memorandums (TAMs) related to audits of credit unions in Alabama and Connecticut. The TAMs identified various revenue sources the IRS considered unrelated business income (UBI). Since the TAMs have been published, they could be considered authority by the IRS for purposes of reporting UBI. The TAMs will be relied upon by IRS agents as guidance in determining what items of income may be subject to unrelated business income tax (UBIT).

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
December 31, 2009 and 2008**

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Income Taxes** (Continued)

As a result, at this time state chartered credit unions should pay income tax on certain types of net taxable income from activities that taxing authorities consider unrelated to the purpose for which the Credit Union was granted non-taxable status. The Credit Union has filed UBIT returns (federal Form 990-T and Form 109 for the state of California) in the past, which has resulted in no unrelated business income taxes paid for the years ended December 31, 2009 and 2008, respectively.

ASC 740-10-65 (Financial Accounting Standards Board Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*, an interpretation of SFAS No. 109) was issued to create a single model to address accounting for uncertainty in tax positions. This standard clarifies the accounting for income taxes by prescribing a minimum recognition threshold a tax position is required to meet before being recognized in the consolidated financial statements. This standard also provides guidance on derecognition, measurement, classification, interest and penalties, disclosure and transition.

The Credit Union adopted this standard on January 1, 2009. As a result of the implementation of this standard, the Credit Union did not recognize any liability for uncertain tax positions.

**Pension Plan – 401(k)**

The Credit Union has a qualified 401(k) plan covering substantially all of its employees.

**Pension Plan – Deferred Compensation Plan [Section 457(b)]**

The Credit Union has a 457(b) non-qualified deferred compensation plan for members of management.

**Advertising Costs**

Advertising costs are charged to operations when incurred.

**Comprehensive Income**

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the consolidated statement of financial condition. For 2009 and 2008, other comprehensive income includes no reclassification adjustments.

**Fair Value Measurements**

Effective January 1, 2008, the Credit Union adopted ASC 820-10-35 (SFAS No. 157, *Fair Value Measurements*), which provides a comprehensive framework for measuring fair value and expands disclosures which are required about fair value measurements. Specifically, this standard sets forth a definition of fair value and establishes a hierarchy prioritizing the inputs to valuation techniques, giving the highest priority to quoted prices in active markets for identical assets and liabilities and the lowest priority to unobservable value inputs. The adoption of this standard did not have a material impact on the Credit Union's December 31, 2008 consolidated financial statements.

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
December 31, 2009 and 2008**

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Subsequent Events**

Management evaluated subsequent events through April 7, 2010, the date the consolidated financial statements were available to be issued. Events or transactions occurring after December 31, 2009, but prior to April 7, 2010 that provided additional evidence about conditions that existed at December 31, 2009, have been recognized in the consolidated financial statements for the year ended December 31, 2009. Events or transactions that provided evidence about conditions that did not exist at December 31, 2009, but arose before the consolidated financial statements were available to be issued, have not been recognized in the consolidated financial statements for the year ended December 31, 2009.

**Reclassifications**

Certain reclassifications have been made to the 2008 consolidated financial statement presentation to correspond to the current year's format. Total equity and net income are unchanged due to these reclassifications.

**NOTE 2 – RESTRICTIONS ON CASH**

The Credit Union is required to maintain balances with corporate credit unions as membership shares that are uninsured and require a notice before withdrawal. Membership share balances were \$719,911 and \$2,500,000 at December 31, 2009 and 2008, respectively.

The Credit Union concluded that the capital shares held in Members United Corporate Federal Credit Union (Members United) and Southwest Corporate Federal Credit Union (Southwest Corporate) were considered impaired and recorded impairment losses totaling \$1,053,294 and \$726,795 for the year ended December 31, 2009. The Credit Union concluded that the capital shares held in Western Corporate Federal Credit Union (WesCorp) were considered impaired and recorded an impairment loss totaling \$8,785,196 for the year ended December 31, 2008.

**NOTE 3 – INVESTMENT SECURITIES**

The amortized cost and estimated fair value of investment securities available-for-sale are as follows:

	<b><u>Amortized Cost</u></b>	<b><u>Gross Unrealized Gains</u></b>	<b><u>Gross Unrealized Losses</u></b>	<b><u>Estimated Fair Value</u></b>
<b>December 31, 2009:</b>				
U.S. government and federal agency securities	\$ 31,133,671	\$ 142,502	\$ (16,255)	\$ 31,259,918
Mortgage-backed securities	<u>16,116,188</u>	<u>51,492</u>	<u>(124,346)</u>	<u>16,043,334</u>
<b>Total</b>	<b><u>\$ 47,249,859</u></b>	<b><u>\$ 193,994</u></b>	<b><u>\$ (140,601)</u></b>	<b><u>\$ 47,303,252</u></b>

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**NOTE 3 – INVESTMENT SECURITIES (CONTINUED)**

	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Estimated Fair Value</u>
<b>December 31, 2008:</b>				
U.S. government and federal agency securities	\$ 20,298,601	\$ 256,818	\$ -	\$ 20,555,419
Mortgage-backed securities	<u>5,792,431</u>	<u>37,681</u>	<u>(2,907)</u>	<u>5,827,205</u>
<b>Total</b>	<u>\$ 26,091,032</u>	<u>\$ 294,499</u>	<u>\$ (2,907)</u>	<u>\$ 26,382,624</u>

At December 31, 2009 and 2008, securities carried at approximately \$42,689,000 and \$21,307,000, respectively, were pledged as collateral against a line of credit with the Federal Home Loan Bank. At December 31, 2009 and 2008, securities carried at approximately \$4,036,000 and \$4,537,000, respectively, were pledged as collateral against a line of credit with the Federal Reserve Bank.

The amortized cost and fair values of investment securities available-for-sale at December 31, 2009 and 2008, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	<u>Available-for-Sale</u>			
	<u>2009</u>		<u>2008</u>	
	<u>Amortized Cost</u>	<u>Estimated Fair Value</u>	<u>Amortized Cost</u>	<u>Estimated Fair Value</u>
Due in one year or less	\$ 2,607,635	\$ 2,627,969	\$ 1,499,954	\$ 1,504,343
Due in one year through five years	<u>28,526,036</u>	<u>28,631,949</u>	<u>18,798,647</u>	<u>19,051,076</u>
	31,133,671	31,259,918	20,298,601	20,555,419
Mortgage-backed securities	<u>16,116,188</u>	<u>16,043,334</u>	<u>5,792,431</u>	<u>5,827,205</u>
<b>Total</b>	<u>\$ 47,249,859</u>	<u>\$ 47,303,252</u>	<u>\$ 26,091,032</u>	<u>\$ 26,382,624</u>

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
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**NOTE 3 – INVESTMENT SECURITIES (CONTINUED)**

Information pertaining to securities with gross unrealized losses at December 31, 2009, aggregated by investment category and length of time that individual investment securities have been in a continuous loss position, are as follows:

<b>Securities available- for sale:</b>	<b><u>Less than 12 Months</u></b>		<b><u>Greater than 12 Months</u></b>	
	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>
U.S. government and federal agency securities	\$ (16,255)	\$ 4,011,112	\$ -	\$ -
Mortgage-backed securities	<u>(124,346)</u>	<u>14,648,161</u>	<u>-</u>	<u>-</u>
<b>Total</b>	<b><u>\$ (140,601)</u></b>	<b><u>\$ 18,659,273</u></b>	<b><u>\$ -</u></b>	<b><u>\$ -</u></b>

At December 31, 2009, there were 12 investment securities with unrealized losses have depreciated 0.75% from the Credit Union's amortized cost basis. All of these securities are either guaranteed by the U.S. Government or secured by mortgage loans. These unrealized losses relate principally to current interest rates for similar types of securities. In analyzing an issue's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition. As management has the ability to hold the securities until maturity, or for the foreseeable future if classified as available-for-sale, no declines are deemed to be other-than-temporary.

Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is possible that changes in the values of investment securities could occur in the near term and that such changes could materially affect the amounts reported in the consolidated statements of financial condition.

Other investment securities at December 31 are summarized as follows:

	<b><u>2009</u></b>	<b><u>2008</u></b>
Funds in corporate credit unions	\$ 184,719,911	\$ 104,245,000
Certificates of deposit with other credit unions	300,000	200,000
Investment in other credit union service organizations	<u>505,234</u>	<u>505,234</u>
<b>Total</b>	<b><u>\$ 185,525,145</u></b>	<b><u>\$ 104,950,234</u></b>

At December 31, 2009, the Credit Union has approximately \$237,755,000 and \$12,330,000 held in accounts at WesCorp and Southwest Corporate. Effective January 28, 2009; all shares, except capital shares, are fully guaranteed by NCUA through a Share Guarantee Program that renews quarterly for a two-year period with a final expiration date of December 31, 2014.

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**NOTE 4 – LOANS TO MEMBERS**

The composition of loans to members at December 31 is as follows:

	<u>2009</u>	<u>2008</u>
Automobile	\$ 149,636,008	\$ 204,206,766
Unsecured	31,567,925	36,426,190
Real estate	286,405,560	335,855,615
Member business	70,814,204	53,284,325
Loan participations	26,188,398	30,206,586
Other	<u>4,426,765</u>	<u>4,446,206</u>
	569,038,860	664,425,688
Net deferred loan origination costs (fees)	(154,666)	10,037
Allowance for loan losses	<u>(14,036,728)</u>	<u>(11,060,194)</u>
<b>Total</b>	<u>\$ 554,847,466</u>	<u>\$ 653,375,531</u>

The Credit Union offers non-traditional mortgage loans to its members. These loans include hybrid and variable interest only mortgages. Hybrid loans consist of loans that are fixed for an initial period of three, five or seven years. After this period, the mortgages are converted to variable rates using an indexed rate, which can result in significant payment shock to the borrower. The interest only loans allow the borrower to pay only interest for a specified number of years. These types of loans may result in a lack of principal amortization or even negative amortization, if the minimum payment is less than the interest accruing on the loan.

Non-traditional mortgage loans may have significantly different credit risk characteristics than traditional fixed and variable rate mortgages. However, the Credit Union believes it has established prudent underwriting standards as well as adequate risk management functions to monitor the additional risk. Non-traditional mortgage loans, which are included in the real estate, member business and loan participation loan captions above, totaled approximately \$67,785,000 and \$85,884,000 at December 31, 2009 and 2008, respectively.

The Credit Union has purchased participations originated by various entities which are secured by commercial property, other real estate and vehicles to members of other credit unions. All of the loan participations were purchased without recourse and the originating entities perform all of the related loan servicing functions on these loans. The automobile loan participations were purchased from WesCorp with limited subordination of up to 5%.

The composition of loan participations at December 31 is as follows:

	<u>2009</u>	<u>2008</u>
Automobile	\$ 148,826	\$ 597,702
Real estate	646,188	992,837
Member business	<u>25,393,384</u>	<u>28,616,047</u>
<b>Total</b>	<u>\$ 26,188,398</u>	<u>\$ 30,206,586</u>

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
December 31, 2009 and 2008**

**NOTE 4 – LOAN TO MEMBERS (CONTINUED)**

A summary of the changes in the allowance for loan losses at December 31 is as follows:

	<u>2009</u>	<u>2008</u>
Balance, beginning of year	\$ 11,060,194	\$ 3,887,923
Provision charged to operations	11,471,792	13,078,520
Loans charged-off	(9,427,920)	(6,523,072)
Recoveries	<u>932,662</u>	<u>616,823</u>
<b>Balance, end of year</b>	<b><u>\$ 14,036,728</u></b>	<b><u>\$ 11,060,194</u></b>

A summary of impaired and non-accrual loans at December 31 is as follows:

	<u>2009</u>	<u>2008</u>
Impaired loans without an allowance	\$ 3,579,000	\$ 1,856,000
Impaired loans with an allowance	<u>22,960,000</u>	<u>8,879,000</u>
<b>Total impaired loans</b>	<b><u>\$ 26,539,000</u></b>	<b><u>\$ 10,735,000</u></b>
Allowance for impaired loans	<u>\$ 4,939,000</u>	<u>\$ 3,625,000</u>
Impaired loans on non-accrual status	<u>\$ 7,248,000</u>	<u>\$ 5,341,000</u>
Non-accrual loans	<u>\$ 9,897,000</u>	<u>\$ 8,209,000</u>
Foregone interest on non-accrual loans	<u>\$ 319,000</u>	<u>\$ 220,000</u>
	<b><u>For the Years Ended December 31,</u></b>	
	<b><u>2009</u></b>	<b><u>2008</u></b>
Average investment in impaired loans	<u>\$ 18,637,000</u>	<u>\$ 5,506,000</u>
Interest income recognized on a cash basis on impaired loans	<u>\$ 1,184,000</u>	<u>\$ 506,000</u>

The interest income recognized on impaired loans approximates the interest income recognized on a cash basis on impaired loans for the years ended December 31, 2009 and 2008.

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
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**NOTE 5 – PREMISES AND EQUIPMENT**

Premises and equipment at December 31 is summarized as follows:

	<u>2009</u>	<u>2008</u>
Land	\$ 5,058,842	\$ 5,058,842
Buildings and improvements	18,161,529	18,188,961
Furniture and equipment	5,448,515	5,004,787
Computer equipment	8,032,630	7,854,335
Leasehold improvements	<u>3,992,118</u>	<u>4,002,251</u>
	40,693,634	40,109,176
Accumulated depreciation and amortization	<u>(17,424,507)</u>	<u>(15,678,159)</u>
<b>Total</b>	<b><u>\$ 23,269,127</u></b>	<b><u>\$ 24,431,017</u></b>

Depreciation and amortization expense amounted to \$1,746,348 and \$1,693,843 for the years ended December 31, 2009 and 2008, respectively.

**NOTE 6 – LEASE COMMITMENTS**

The Credit Union leases certain office facilities under noncancelable operating leases expiring in various years through 2016. Some of the leases contain renewal options for periods from three to five years at their fair rental value at the time of renewal. Future minimum lease payments under these leases are as follows:

**Years Ending December 31,**

2010	\$ 707,179
2011	584,361
2012	502,298
2013	273,430
2014	186,226
Thereafter	<u>165,854</u>
<b>Future minimum lease payments</b>	<b><u>\$ 2,419,348</u></b>

Minimum lease payments exclude rentals under renewal options, which, as of December 31, 2009, are not reasonably assured of being exercised.

Rent expense was approximately \$790,000 and \$737,000 for the years ended December 31, 2009 and 2008, respectively.

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
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**NOTE 7 – MEMBERS' SHARE AND SAVINGS ACCOUNTS**

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

	<u>2009</u>	<u>2008</u>
Regular share accounts	\$ 165,822,430	\$ 145,874,487
Share draft accounts	127,459,509	109,697,876
Money market accounts	221,094,166	171,517,147
IRA share accounts	<u>5,375,503</u>	<u>4,913,262</u>
Total share accounts	<u>519,751,608</u>	<u>432,002,772</u>
Share and IRA certificates		
0.00% to 1.99%	236,198,603	-
2.00% to 2.99%	27,201,247	97,787,234
3.00% to 3.99%	19,992,023	197,510,853
4.00% to 4.99%	12,153,786	46,266,145
5.00% to 5.99%	14,432,257	22,278,096
6.00% to 6.99%	<u>200,511</u>	<u>462,176</u>
Total certificate accounts	<u>310,178,427</u>	<u>364,304,504</u>
<b>Total members' share and savings accounts</b>	<b><u>\$ 829,930,035</u></b>	<b><u>\$ 796,307,276</u></b>

Scheduled maturities of share and IRA certificates at December 31, 2009 are as follows:

**Years Ending December 31,**

2010	\$ 255,358,982
2011	29,602,521
2012	12,358,311
2013	5,411,590
2014	7,420,347
Thereafter	<u>26,676</u>
<b>Total certificate accounts</b>	<b><u>\$ 310,178,427</u></b>

The aggregate amounts of members' share and savings accounts in denominations of \$100,000 or more were approximately \$346,747,000 and \$343,850,000 at December 31, 2009 and 2008, respectively.

Overdrawn share accounts reclassified to other assets totaled \$344,050 and \$395,111 at December 31, 2009 and 2008, respectively.

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
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**NOTE 8 – LINE OF CREDIT**

The Credit Union maintains lines of credit with WesCorp, the Federal Home Loan Bank of San Francisco (FHLB) and the Federal Reserve Bank of San Francisco (FRB) as described below:

<u>December 31, 2009</u>	<u>WesCorp Settlement</u>	<u>WesCorp Variable/Fixed</u>	<u>FHLB</u>	<u>FRB</u>	<u>Total Lines</u>
Total available	\$ 95,000,000	\$ 60,000,000	\$216,601,983	\$ 3,952,634	\$375,554,617
Borrowed	<u>-</u>	<u>-</u>	<u>(13,000,000)</u>	<u>-</u>	<u>(13,000,000)</u>
<b>Remaining available</b>	<u>\$ 95,000,000</u>	<u>\$ 60,000,000</u>	<u>\$203,601,983</u>	<u>\$ 3,952,634</u>	<u>\$362,554,617</u>
Term	LOC	LOC	LOC	LOC	
Weighted average rate	N/A	N/A	3.74%	N/A	

  

<u>December 31, 2008</u>	<u>WesCorp Settlement</u>	<u>WesCorp Variable/Fixed</u>	<u>FHLB</u>	<u>FRB</u>	<u>Total Lines</u>
Total available	\$ 95,000,000	\$ 60,000,000	\$223,358,113	\$ 4,407,645	\$382,765,758
Borrowed	<u>-</u>	<u>-</u>	<u>(14,250,000)</u>	<u>-</u>	<u>(14,250,000)</u>
<b>Remaining available</b>	<u>\$ 95,000,000</u>	<u>\$ 60,000,000</u>	<u>\$209,108,113</u>	<u>\$ 4,407,645</u>	<u>\$368,515,758</u>
Term	LOC	LOC	LOC	LOC	
Weighted average rate	N/A	N/A	3.77%	N/A	

The WesCorp settlement line is collateralized by substantially all of the Credit Union's assets, excluding assets pledged to secure other lines of credit as described below. The WesCorp variable/fixed line is collateralized by WesCorp certificate of deposit balances totaling approximately \$170,500,000 and \$74,500,000 at December 31, 2009 and 2008, respectively. The FHLB line is collateralized by federal agency and mortgage-backed securities held in safekeeping by the FHLB and certain residential first mortgage, second mortgage, home equity lines of credit and commercial real estate loans. The outstanding principle balance of real estate loans pledged as collateral to the FHLB totaled approximately \$376,660,000 and \$403,621,000 at December 31, 2009 and 2008, respectively. The FRB line of credit is collateralized by federal agency securities held in safekeeping by the FRB.

**NOTE 9 – BORROWED FUNDS**

Borrowed funds at December 31 are as follows:

	<u>2009</u>	<u>2008</u>
FHLB, fixed rate (3.74% and 3.77% weighted average rates at December 31, 2009 and 2008, respectively), secured, with various maturity dates	\$ 13,000,000	\$ 14,250,000
Note payable to City of Buena Park, interest free, secured	<u>100,000</u>	<u>100,000</u>
<b>Total</b>	<u>\$ 13,100,000</u>	<u>\$ 14,350,000</u>

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**NOTE 9 – BORROWED FUNDS (CONTINUED)**

The note payable to the City of Buena Park is an interest free loan to pay for the construction of a Credit Union branch. The borrowing is due and payable if the building is sold.

Scheduled maturities of borrowed funds at December 31, 2009, are as follows:

**Years Ending December 31,**

2010	\$ 2,000,000
2011	2,500,000
2012	1,500,000
2013	4,000,000
2014	-
2015	<u>3,000,000</u>
	13,000,000
No scheduled maturity	<u>100,000</u>
<b>Total</b>	<b><u>\$ 13,100,000</u></b>

**NOTE 10 – ADVERTISING**

Advertising expense totaled approximately \$480,000 and \$854,000 for the years ended December 31, 2009 and 2008, respectively.

**NOTE 11 – OFF-BALANCE SHEET ACTIVITIES**

The Credit Union is a party to conditional commitments to lend funds in the normal course of business to meet the financing needs of its members. These commitments represent financial instruments to extend credit which include lines of credit, credit cards, home equity lines, and overdraft protection commitments that involve, to varying degrees, elements of credit and interest rate risk in excess of amounts recognized in the consolidated financial statements.

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

At December 31, the following financial instruments were outstanding whose contract amounts represent credit risk:

	<b><u>2009</u></b>	<b><u>2008</u></b>
Commitments to grant loans:		
Home-equity lines of credit	\$ 43,075,365	\$ 47,464,564
Credit cards	4,766,524	3,361,296
Line-of-credit loans	31,641,682	33,123,688
Overdraft protection program commitments	<u>7,118,379</u>	<u>6,718,241</u>
<b>Total</b>	<b><u>\$ 86,601,950</u></b>	<b><u>\$ 90,667,789</u></b>

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
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**NOTE 11 – OFF-BALANCE SHEET ACTIVITIES (CONTINUED)**

Commitments to extend credit are agreements to lend to a member as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Because many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Credit Union evaluates each member's creditworthiness on a case-by-case basis. The amount of collateral obtained if deemed necessary by the Credit Union upon extension of credit is based on management's credit evaluation of the counterparty. Collateral held varies but may include consumer assets, residential real estate and member share balances.

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

**NOTE 12 – LEGAL CONTINGENCIES**

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

**NOTE 13 – CAPITAL REQUIREMENTS**

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

Quantitative measures established by regulation to ensure capital adequacy require the Credit Union to maintain minimum amounts and ratios (set forth in the following table) of net worth (as defined in the regulations) to assets and RBNW ratios (as defined). As of December 31, 2009 and 2008, the Credit Union's RBNW requirement was 4.36% and 4.45%, respectively. The minimum ratio to be considered complex under the regulatory framework is 6 percent. Management believes that, as of December 31, 2009, the Credit Union meets all capital adequacy requirements to which it is subject. No conditions or events have occurred since the calculation date that management believes has changed the Credit Union's category.

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**NOTE 13 – CAPITAL REQUIREMENTS (CONTINUED)**

As of December 31, 2009, the most recent call reporting period, the NCUA has categorized the Credit Union as well capitalized under the regulatory framework for Prompt Corrective Action. To be categorized as well capitalized, the Credit Union must maintain a minimum net worth ratio of 7%. The Credit Union's actual capital amounts and ratios as of December 31, 2009 and 2008 are also presented in the table.

The Credit Union's actual capital amounts and ratios as of December 31, 2009 are as follows:

	<u>Actual</u>		<u>To Be Adequately Capitalized Under Prompt Corrective Action Provisions</u>		<u>To Be Well Capitalized Under Prompt Corrective Action Provisions</u>	
	<u>Amount</u>	<u>Ratio</u>	<u>Amount</u>	<u>Ratio</u>	<u>Amount</u>	<u>Ratio</u>
Net worth	\$ 78,607,796	8.59%	\$ 54,897,610	6.0%	\$ 64,047,212	7.0%
Risk-based net worth requirement	\$ 39,892,263	4.36%	N/A	N/A	N/A	N/A

Because the RBNW ratio of 4.36% is less than the net worth ratio of 8.59%, the Credit Union retains its original category. Further, in performing its calculation of total assets, the Credit Union used the average of the current and three preceding calendar quarter-end balances option, as permitted by regulation.

The Credit Union's actual capital amounts and ratios as of December 31, 2008 are as follows:

	<u>Actual</u>		<u>To Be Adequately Capitalized Under Prompt Corrective Action Provisions</u>		<u>To Be Well Capitalized Under Prompt Corrective Action Provisions</u>	
	<u>Amount</u>	<u>Ratio</u>	<u>Amount</u>	<u>Ratio</u>	<u>Amount</u>	<u>Ratio</u>
Net worth	\$ 79,033,574	8.85%	\$ 53,605,947	6.0%	\$ 62,540,272	7.0%
Risk-based net worth requirement	\$ 39,757,744	4.45%	N/A	N/A	N/A	N/A

**NOTE 14 – RELATED PARTY TRANSACTIONS**

In the normal course of business, the Credit Union extends credits to members of the Board of Directors, Supervisory Committee members and executive officers. The aggregate loans to related parties at December 31, 2009 and 2008 were approximately \$4,257,000 and \$4,839,000, respectively. Deposits from related parties at December 31, 2009 and 2008 amounted to approximately \$1,786,000 and \$2,336,000, respectively.

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
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**NOTE 15 – 401(k) RETIREMENT PLAN**

The Credit Union provides a 401(k) employee benefit plan covering substantially all employees who have completed at least one year of service and met minimum age requirements. The Credit Union matches a portion of employees' wage reductions. Total pension expense under this plan was \$880,614 and \$859,050 for the years ended December 31, 2009 and 2008, respectively.

**NOTE 16 – DEFERRED COMPENSATION PLAN [SECTION 457(b)]**

The Credit Union has a 457(b) non-qualified deferred compensation plan for members of management. The Credit Union makes discretionary contributions to the plan and employees are allowed to contribute to the plan. The deferred compensation accounts are shown as both assets and liabilities on the Credit Union's consolidated financial statements and are available to creditors in the event of the Credit Union's liquidation.

The balance of the deferred compensation arrangement, included in other assets and accrued expenses and other liabilities on the consolidated statements of financial condition, was \$188,230 and \$143,857 as of December 31, 2009 and 2008, respectively.

**NOTE 17 – FAIR VALUES OF FINANCIAL INSTRUMENTS**

The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Credit Union's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument. The aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Credit Union.

The following methods and assumptions were used by the Credit Union in estimating fair values of financial instruments as disclosed herein:

**Cash and Cash Equivalents:** The carrying amounts of cash and cash equivalents approximate their fair value.

**Available-For-Sale Securities:** Market value technique is marked to market on a monthly basis, of which information is performed and provided on monthly basis by Morgan Keegan. Month end market prices are obtained through the Morgan Keegan report folio investment accounting service. Morgan Keegan obtains their market values from Reuters. Reuters methodology for the valuation of U.S. Government and Federal Agency Securities is based on an OAS model, which includes the LIBOR/Swap forward curve, credit spreads and interest rate volatilities. The valuation of seasoned mortgage-backed securities pools is based on market makers and live trading systems. The valuation of mortgage-backed securities adjustable rate mortgages is based on the bond equivalent effective margin. These figures are validated by comparing Morgan Keegan results to the primary safekeeper, Federal Home Loan Bank.

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
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December 31, 2009 and 2008**

**NOTE 17 – FAIR VALUES OF FINANCIAL INSTRUMENTS (CONTINUED)**

**Other Investment Securities:** The carrying amounts of other investment securities approximate their fair value.

**Federal Home Loan Bank Stock:** The carrying amount of the Federal Home Loan Bank stock approximates the fair value.

**Loans Held-for-Sale:** Mortgage loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated market value in the aggregate.

**Loans to Members:** For variable-rate loans that reprice frequently and have no significant change in the 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 based on quoted market prices of similar loans sold in conjunction with securitization transactions, adjusted for differences in loan characteristics; or are based on estimated cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Fair values for business real estate and business loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Fair values for impaired loans are estimated using discounted cash flow analyses or underlying collateral value, where appropriate.

**Accrued Interest Receivable:** The carrying amounts of accrued interest receivable approximate their fair value.

**Foreclosed Assets:** The carrying amounts of foreclosed assets approximate their fair value.

**Members' Share and Savings Accounts:** The fair values disclosed for share draft, regular savings 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 variable-rate, fixed-term share certificates approximate their fair values at the reporting date. Fair values for fixed-rate 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 share certificates.

**Borrowed Funds:** The carrying amounts of borrowed funds maturing within 90 days approximate their fair values. Fair values of other borrowed funds are estimated using discounted cash flow analyses based on the Credit Union's current incremental borrowing rates for similar types of borrowing arrangements.

**Off-Balance-Sheet Instruments:** The estimated fair value of the commitments to extend credit represents the Credit Union's potential unfunded commitments under such lines-of-credit.

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**NOTE 17 – FAIR VALUES OF FINANCIAL INSTRUMENTS (CONTINUED)**

The estimated fair values of the Credit Union's financial instruments, none of which are held for trading purposes, are as follows:

	<u>2009</u>		<u>2008</u>	
	<u>Carrying Amount</u>	<u>Fair Value</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
<b>FINANCIAL ASSETS</b>				
Cash and cash equivalents	\$ 89,656,852	\$ 89,657,000	\$ 65,977,711	\$ 65,978,000
Investment securities:				
Available-for-sale	47,303,252	47,303,000	26,382,624	26,383,000
Other investments	185,525,145	185,525,000	104,950,234	104,950,000
FHLB stock	3,550,900	3,551,000	3,219,600	3,220,000
Loans held-for-sale	5,248,538	5,249,000	981,000	981,000
Loans to members, net of allowance for loan losses	554,847,466	565,232,000	653,375,531	660,330,000
Accrued interest receivable	2,604,946	2,605,000	3,137,933	3,138,000
Foreclosed assets	725,775	726,000	1,139,195	1,139,000
<b>FINANCIAL LIABILITIES</b>				
Members' share and savings accounts:				
Share, drafts, and money market accounts	\$ 519,751,608	\$ 519,752,000	\$ 432,002,772	\$ 432,003,000
Certificate accounts	310,178,427	312,711,000	364,304,504	369,342,000
Borrowed funds	13,100,000	13,463,000	14,350,000	14,740,000
<b>UNRECOGNIZED FINANCIAL INSTRUMENTS</b>				
Commitments to extend credit	\$ -	\$ 86,602,000	\$ -	\$ 90,668,000

**NOTE 18 – FAIR VALUE OF FINANCIAL INSTRUMENTS MEASUREMENTS**

In determining fair value, the Credit Union uses various valuation approaches within the ASC 820-10-35 (FAS No. 157) fair value measurement framework. Fair value measurements are determined based on the assumptions that market participants would use in pricing an asset or liability.

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
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**NOTE 18 – FAIR VALUE OF FINANCIAL INSTRUMENTS MEASUREMENTS (CONTINUED)**

This standard establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. This standard defines levels within the hierarchy based on the reliability of inputs as follows:

- Level 1 Valuations based on unadjusted quoted prices for identical assets or liabilities in active markets;
- Level 2 Valuations based on quoted prices for similar assets or liabilities or identical assets or liabilities in less active markets, such as dealer or broker markets; and
- Level 3 Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable, such as pricing models, discounted cash flow models and similar techniques not based on market, exchange, dealer or broker-traded transactions.

Following is a description of the valuation methodologies used for instruments measured at fair value and their classification in the valuation hierarchy.

**Available-For-Sale Investments:** Market value technique is marked to market on a monthly basis, of which information is performed and provided on monthly basis by Morgan Keegan. Month end market prices are obtained through the Morgan Keegan report folio investment accounting service. Morgan Keegan obtains their market values from Reuters. Reuters methodology for the valuation of U.S. Government and Federal Agency Securities is based on an OAS model, which includes the LIBOR/Swap forward curve, credit spreads and interest rate volatilities. The valuation of seasoned mortgage-backed securities pools is based on market makers and live trading systems. The valuation of mortgage-backed securities adjustable rate mortgages is based on the bond equivalent effective margin. These figures are validated by comparing Morgan Keegan results to the primary safekeeper, Federal Home Loan Bank.

**Impaired Loans and Foreclosed Assets:** The fair value of impaired loans and foreclosed assets is generally based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available.

	<b><u>Fair Value Measurements at Reporting Date Using</u></b>			
		<b>Quoted Prices in Active Markets for Identical Assets/Liabilities (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>
	<b><u>Total Fair Value</u></b>			
<b>December 31, 2009</b>				
Available-for-sale securities	\$ 47,303,000	\$ -	\$ 47,303,000	\$ -
<b>December 31, 2008</b>				
Available-for-sale securities	\$ 26,383,000	\$ -	\$ 26,383,000	\$ -

**ORANGE COUNTY'S CREDIT UNION AND SUBSIDIARY  
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**NOTE 18 – FAIR VALUE OF FINANCIAL INSTRUMENTS MEASUREMENTS (CONTINUED)**

Fair values of assets and liabilities measured on a non-recurring basis at December 31 are as follows:

	<b><u>Fair Value Measurements at Reporting Date Using</u></b>			
		<b>Quoted Prices in Active Markets for Identical Assets/Liabilities (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>
	<b><u>Fair Value</u></b>			
<b><i>December 31, 2009</i></b>				
Impaired loans	\$ 21,600,000	\$ -	\$ -	\$ 21,600,000
Foreclosed assets	726,000	-	-	726,000
<b><i>December 31, 2008</i></b>				
Impaired loans	\$ 7,110,000	\$ -	\$ -	\$ 7,110,000
Foreclosed assets	1,139,000	-	-	1,139,000

This information is an integral part of the accompanying consolidated financial statements.