

**NORTHCOUNTRY COOPERATIVE  
DEVELOPMENT FUND**

**FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED  
DECEMBER 31, 2013 AND 2012**



NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

FINANCIAL STATEMENTS

For the Years Ended December 31, 2013 and 2012

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## INDEPENDENT AUDITOR'S REPORT

Board of Directors and Members  
Northcountry Cooperative Development Fund  
Minneapolis, Minnesota

We have audited the accompanying financial statements of Northcountry Cooperative Development Fund, which comprise the balance sheets as of December 31, 2013 and 2012, and the related statements of operations, stockholders' equity, and cash flows for the years then ended, and the related notes to financial statements.

### **Management's Responsibility for the Financial Statements**

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

### **Auditor's Responsibility**

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

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

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

## Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Northcountry Cooperative Development Fund as of December 31, 2013 and 2012, 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.

## Uncertainties Regarding the Deferred Income Tax Asset

As discussed in Note 10, Northcountry Cooperative Development Fund has recorded a \$200,200 deferred income tax asset at December 31, 2013 and 2012. Utilization of the deferred income tax asset is dependent upon Northcountry Cooperative Development Fund generating sufficient income within the net operating loss carryforward period. As discussed in Note 11, management's projection of future income is heavily dependent upon future grant revenues. Due to the uncertainty of future income, it is at least reasonably possible that management's view of future income will change in the near term. Our opinion is not modified with respect to that matter.

Saint Paul, Minnesota  
April 17, 2014

*Maloney Ulbrich*  
*Christianese Rues P.A.*

NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

BALANCE SHEETS

December 31, 2013 and 2012

	2013	2012
<b>ASSETS</b>		
Cash and cash equivalents	\$ 1,039,975	\$ 628,438
Funds held for KSCR	116,136	43,840
Loans receivable	7,016,557	6,143,359
Less allowance for loan losses	(380,025)	(343,082)
Loans receivable, net	6,636,532	5,800,277
Accrued interest receivable	25,874	21,966
Other receivables	-	122
Prepaid expenses	5,729	5,453
Office equipment, net	10,182	20,279
Deferred income tax asset	200,200	200,200
Total assets	\$ 8,034,628	\$ 6,720,575
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Notes payable and accrued interest	\$ 7,636,875	\$ 6,401,803
Funds due to KSCR	116,136	43,840
Accounts payable	9,600	27,890
Accrued expenses	8,603	4,222
Total liabilities	7,771,214	6,477,755
Stockholders' equity:		
Preferred stock, \$10 par value, 500,000 shares authorized, 102,596 and 97,596 shares outstanding in 2013 and 2012, respectively	1,025,960	975,960
Common stock - voting, \$10 par value, 1,000 shares authorized, 471 and 477 shares outstanding in 2013 and 2012, respectively	4,710	4,770
Common stock - nonvoting, \$10 par value, 500,000 shares authorized, 48,500 and 48,500 shares outstanding in 2013 and 2012, respectively	485,000	485,000
Additional paid-in capital	495,489	464,664
Retained earnings (accumulated deficit)	(1,747,745)	(1,687,574)
Total stockholders' equity	263,414	242,820
Total liabilities and stockholders' equity	\$ 8,034,628	\$ 6,720,575

See accompanying notes to financial statements.

NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

STATEMENTS OF OPERATIONS

For the Years Ended December 31, 2013 and 2012

	2013	2012
Interest income:		
Loans receivable	\$ 486,295	\$ 431,822
Operating cash investments	893	2,190
Total interest income	487,188	434,012
Interest expense	(155,997)	(158,055)
Net interest income	331,191	275,957
Provision for loan losses, net	(36,943)	(58,197)
Net interest income after provision for loan losses	294,248	217,760
Noninterest income:		
Fees and service charges	48,663	49,694
Grant revenue	16,112	1,019
Other income	221	942
Total noninterest income	64,996	51,655
Income before noninterest expenses	359,244	269,415
Noninterest expenses:		
Compensation and employee benefits	237,727	233,318
Contract services	112,489	100,870
Office	21,141	30,087
Advertising	10,373	5,743
Depreciation	10,097	9,328
Occupancy	9,200	18,843
Other	18,388	20,585
Expense reimbursements - affiliates	-	(16,397)
Total noninterest expenses	419,415	402,377
Loss before income taxes	(60,171)	(132,962)
Income tax expense	-	-
Net loss	\$ (60,171)	\$ (132,962)

See accompanying notes to financial statements.

NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

STATEMENTS OF STOCKHOLDERS' EQUITY

For the Years Ended December 31, 2013 and 2012

	Preferred Stock		Common Stock - Voting		Common Stock - Nonvoting		Additional Paid-In Capital	Retained Earnings (Accumulated Deficit)	Total Stockholders' Equity
	Shares	Amount	Shares	Amount	Shares	Amount			
Balance, December 31, 2011	47,892	\$ 478,922	483	\$ 4,830	48,502	\$ 485,020	\$ 395,392	\$ (1,548,632)	\$ (184,468)
Preferred stock:									
Transfer from notes payable	50,000	500,000	-	-	-	-	-	-	500,000
Reclassification of patronage dividend	(296)	(2,962)	-	-	-	-	2,962	-	-
Common stock:									
Issuance of common stock	-	-	12	120	-	-	9,360	-	9,480
Redemption of common stock	-	-	(3)	(30)	-	-	(230)	-	(260)
Reclassification	-	-	(15)	(150)	(2)	(20)	6,150	(5,980)	-
Capital contributions	-	-	-	-	-	-	51,030	-	51,030
Net loss	-	-	-	-	-	-	-	(132,962)	(132,962)
Balance, December 31, 2012	97,596	975,960	477	4,770	48,500	485,000	464,664	(1,687,574)	242,820
Preferred stock:									
Transfer from notes payable	5,000	50,000	-	-	-	-	-	-	50,000
Common stock:									
Issuance of common stock	-	-	16	160	-	-	19,640	-	19,800
Redemption of common stock	-	-	(28)	(280)	-	-	-	-	(280)
Reclassification	-	-	6	60	-	-	(60)	-	-
Capital contributions	-	-	-	-	-	-	11,245	-	11,245
Net loss	-	-	-	-	-	-	-	(60,171)	(60,171)
Balance, December 31, 2013	102,596	\$ 1,025,960	471	\$ 4,710	48,500	\$ 485,000	\$ 495,489	\$ (1,747,745)	\$ 263,414

See accompanying notes to financial statements.



NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

STATEMENTS OF CASH FLOWS

For the Years Ended December 31, 2013 and 2012  
Increase (Decrease) in Cash and Cash Equivalents

	<u>2013</u>	<u>2012</u>
Cash flows from operating activities:		
Net loss	\$ (60,171)	\$ (132,962)
Adjustments to reconcile net loss to net cash from operating activities:		
Depreciation	10,097	9,328
Provision for loan losses	36,943	58,197
Changes in operating assets and liabilities:		
Receivables	(3,786)	3,252
Prepaid expenses	(276)	(3,587)
Accounts payable	(18,290)	23,784
Accrued interest	38,808	(6,726)
Accrued expenses	4,381	(6,058)
Net cash from operating activities	<u>7,706</u>	<u>(54,772)</u>
Cash flows from investing activities:		
Collections on loans receivable	896,671	1,912,748
Issuance of loans receivable	(1,769,869)	(1,187,971)
Purchase of office equipment	-	(6,986)
Net cash from investing activities	<u>(873,198)</u>	<u>717,791</u>
Cash flows from financing activities:		
Issuance of notes payable	1,790,264	88,857
Repayments on notes payable	(539,000)	(802,227)
Proceeds from issuance of common stock	14,800	9,480
Proceeds from additional paid in capital contribution	11,245	51,030
Redemption of common stock	(280)	(260)
Net cash from financing activities	<u>1,277,029</u>	<u>(653,120)</u>
Net increase in cash and cash equivalents	411,537	9,899
Cash and cash equivalents - beginning of year	<u>628,438</u>	<u>618,539</u>
Cash and cash equivalents - end of year	<u>\$ 1,039,975</u>	<u>\$ 628,438</u>
Supplemental disclosures of cash flow information:		
Cash paid for interest	<u>\$ 117,837</u>	<u>\$ 164,781</u>
Stock issued in exchange for notes payable	<u>\$ 55,000</u>	<u>\$ 500,000</u>

See accompanying notes to financial statements.

# NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

## NOTES TO FINANCIAL STATEMENTS

For the Years Ended December 31, 2013 and 2012

### 1. ORGANIZATION

Northcountry Cooperative Development Fund (NCDF) is a member-owned and member-governed financial intermediary providing loans to support the growth and development of cooperative enterprises. NCDF provides financing to consumer, worker, housing and producer cooperatives and their members throughout the United States.

NCDF obtains funds from its members as well as from non-member institutions interested in supporting the cooperative economy, including foundations, religious organizations, community groups, cooperative coalitions, financial institutions and socially responsible organizations.

NCDF was formed in 1978 and is organized as a cooperative association under Chapter 308A of Minnesota law and is certified as a Community Development Financial Institution (CDFI) by the United States Department of Treasury.

NCDF has more than 165 member cooperatives and more than 250 individual members in 31 states.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Use of Estimates** - The preparation of 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to material change are the allowance for loan losses and the valuation allowance for the deferred income tax asset.

**Cash Equivalents** - NCDF considers all investment instruments purchased with original maturities of three months or less to be cash equivalents.

**Credit Risk** - Financial instruments that potentially subject NCDF to credit risk include cash on deposit at banks. NCDF has not experienced any losses in such accounts. As of December 31, 2013 and 2012, balances exceed the insured limits by approximately \$687,000 and \$169,000 respectively. NCDF does not believe it is exposed to any significant concentration of credit risk on cash.

Additionally, loans receivable subject NCDF to a credit risk. Generally, loans are collateralized by property, equipment and inventory of the borrower.

**Loans Receivable** - NCDF provides commercial and cooperative home ownership (share) loans to members throughout the United States. The ability of the members to honor their contracts is dependent upon sound management of the cooperative, general economic conditions and the value of real estate collateral in the member's geographic area.

(Continued)

NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

NOTES TO FINANCIAL STATEMENTS

For the Years Ended December 31, 2013 and 2012

2. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Loans receivable are stated at unpaid principal balances, less an allowance for loan losses. Interest on loans is recognized over the term of the loan and is calculated using the simple-interest method on principal amounts outstanding. The accrual of interest on loans is discontinued at the time the loan is 120 days delinquent unless the credit is well-secured and in process of collection.

Loans are placed on non-accrual status or charged off if all or a portion of the loan is deemed to be uncollectible by management based on economic conditions, business conditions and collection efforts. It is NCDF's policy that any loan that is more than 120 days delinquent shall be charged off unless management determines that pay off of the loan is imminent, whether through collections, liquidation or foreclosure. The Board of Directors must approve the charge off of any loan, generally upon recommendation from the Loan and Finance Committees.

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

Non-refundable commitment fees are recognized upon receipt. Loan fees are recognized as income upon closing of the loan because incremental direct costs incurred on each loan exceed the fees charged.

**Allowance for Loan Losses** - The allowance for loan losses is a non-cash reserve established against potential or expected losses on loans. Each loan in the portfolio is assigned a risk rating and each rating has a corresponding percentage that must be set aside as an allowance. The ratings and the allowance are evaluated regularly by management based upon qualitative factors that are subjective and require a high degree of management judgment. These factors include adverse situations that may affect the borrower's ability to repay, estimated value of the underlying collateral and prevailing economic conditions. The Loan Committee establishes initial risk ratings at the time loans are approved and must approve any changes to ratings. In addition, on a quarterly basis, the Loan Committee reviews and approves all risk ratings and the allowance for loan losses. The Board of Directors reviews the allowance and risk ratings at least annually.

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 loan is uncollectible. Subsequent recoveries are credited to income.

(Continued)

NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

NOTES TO FINANCIAL STATEMENTS

For the Years Ended December 31, 2013 and 2012

2. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Office Equipment** - Office equipment is capitalized at cost. Depreciation is provided using the straight-line method over estimated useful lives of three to seven years. When an asset is retired or sold, its cost and related accumulated depreciation are removed from the account and the resulting gain or loss is reflected in the statement of operations. Accumulated depreciation was \$47,663 and \$37,566 as of December 31, 2013 and 2012.

**Fair Value Measurements** - NCDF determines fair value, when necessary, based on the assumptions that market participants would use when pricing the asset or liability. NCDF does not currently have any financial assets or liabilities that are measured at fair value on a recurring or non-recurring basis.

**Income Taxes** - NCDF is taxed as a cooperative and is subject to the provisions of Subchapter T of the Internal Revenue Code. The bylaws require NCDF to annually distribute net income from patronage to its members, based on their patronage with NCDF. The distributions may be in the form of cash, stock or allocated surplus, which reduces NCDF's income tax liability. However, losses in NCDF's patronage business may, at the Board's discretion, be carried forward to offset future distributions of net income from patronage. Members of NCDF receiving qualified patronage dividends consent to include them in their taxable income.

Income taxes are provided for the tax effects of the transactions reported in the financial statements and consist of taxes currently due plus deferred income taxes related primarily to the difference between the basis of loans receivable for financial and income tax reporting, which consists of the allowance for loan losses. The deferred income tax asset includes the future tax return consequences of that difference, which will be deductible when the loans are written off. A deferred income tax asset is also recognized for operating losses that are available to offset future taxable income. The deferred income taxes are reflected at income tax rates applicable to the period in which the deferred income taxes are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred income taxes are adjusted through the provision for income taxes. If it is more likely than not that all or some portion of the deferred income tax asset will not be realized, a valuation allowance is recognized.

Federal and state tax authorities generally have the right to examine income tax returns for a period of three years after they are filed. The Cooperative is not currently under examination by any taxing jurisdiction. Any interest or penalties associated with income tax positions are reported in other noninterest expenses. There were no such interest or penalties in 2013 and 2012.

(Continued)

NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

NOTES TO FINANCIAL STATEMENTS

For the Years Ended December 31, 2013 and 2012

2. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Reclassifications** - Certain reclassifications have been made to the prior year financial statements to be consistent with the current year classifications. The reclassifications did not change the net loss or stockholders' equity.

3. **LOANS RECEIVABLE**

The following table presents the recorded investment in loans, net of participations, by portfolio segment and the allowance for loan losses as of December 31:

	<u>2013</u>	<u>2012</u>
Cooperative housing mortgage loans	\$ 3,256,609	\$ 3,070,905
Cooperative business mortgage loans	1,129,929	1,023,549
Cooperative business loans	2,336,112	1,734,337
Loans to individuals to purchase cooperative housing	<u>293,907</u>	<u>314,568</u>
Total loans	7,016,557	6,143,359
Less allowance for loan losses	<u>(380,025)</u>	<u>(343,082)</u>
	<u>\$ 6,636,532</u>	<u>\$ 5,800,277</u>

The following table presents the change in the allowance for loan losses in 2013 and 2012:

Beginning balance	\$ 343,082	\$ 284,885
Provision for loan losses	36,943	58,197
Loans charged off	-	-
Ending balance	<u>\$ 380,025</u>	<u>\$ 343,082</u>

In addition to the loans summarized above, NCDF services the following loan participations:

Loan participations serviced	<u>\$ 1,159,337</u>	<u>\$ 991,331</u>
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(Continued)

NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

NOTES TO FINANCIAL STATEMENTS

For the Years Ended December 31, 2013 and 2012

3. **LOANS RECEIVABLE (Continued)**

The following table presents the aging of loans by portfolio segment at December 31, 2013:

	Cooperative housing mortgage loans	Cooperative business mortgage loans	Cooperative business loans	Loans to individuals to purchase cooperative housing	Total
Current	\$ 3,256,609	\$ 984,559	\$ 2,336,112	\$ 293,907	\$ 6,871,187
31 - 90	-	145,370	-	-	145,370
90 + days	-	-	-	-	-
Total	<u>\$ 3,256,609</u>	<u>\$ 1,129,929</u>	<u>\$ 2,336,112</u>	<u>\$ 293,907</u>	<u>\$ 7,016,557</u>

The following table presents the allowance for loan losses by portfolio segment in 2013:

Beginning balance	\$ 219,338	\$ 54,490	\$ 62,803	\$ 6,451	\$ 343,082
Provision	5,848	10,125	21,860	(890)	36,943
Ending balance	<u>\$ 225,186</u>	<u>\$ 64,615</u>	<u>\$ 84,663</u>	<u>\$ 5,561</u>	<u>\$ 380,025</u>

The following table and the accompanying explanations present informative data regarding the credit quality of loans receivable at December 31, 2013:

A	\$ 1,612,045	\$ 530,002	\$ -	\$ 176,076	\$ 2,318,123
B	962,762	351,205	1,732,097	64,656	3,110,720
C	361,336	103,352	554,015	43,563	1,062,266
D	-	-	50,000	-	50,000
F	320,466	145,370	-	9,612	475,448
	<u>\$ 3,256,609</u>	<u>\$ 1,129,929</u>	<u>\$ 2,336,112</u>	<u>\$ 293,907</u>	<u>\$ 7,016,557</u>

The following categories are used to assess the risk profile of the loan portfolio:

Category	Description of Creditworthiness	Allowance %
A	Highest credit quality, borrower is stable and reliable	0 - 1
B	Good borrower, but some recent internal or external changes	1.5 - 5
C	Good borrower, but recent significant internal or external changes and challenges	3 - 5
D	Borrower is either rebounding or heading into a period of significant difficulties	6 - 10
E	Relatively weak borrower facing some internal or external challenges	10 - 15
F	Weak borrower facing significant challenges	25 plus
G	Doubtful	Up to 100

(Continued)

NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

NOTES TO FINANCIAL STATEMENTS

For the Years Ended December 31, 2013 and 2012

3. **LOANS RECEIVABLE (Continued)**

Loans are considered impaired if it is probable that at least some of the principal and interest payments will not be collected. Other information related to loan impairment as of December 31, 2013 follows:

- All loans are individually reviewed for impairment
- Management has determined that there are no impaired loans
- Management is in the process of reviewing one loan for restructuring
- There are no loans on non-accrual status

4. **KSCR FUNDS**

NCDF entered into an agreement with NASCO Development Services to provide loan servicing functions for their KSCR Fund. NCDF accumulates principal and interest collections, net of remitting interest due to investors of the KSCR Fund, for use in providing additional loans on behalf of the KSCR Fund. NASCO Development Services and the KSCR Fund investors bear all risk of loss pertaining to these loans.

At December 31, 2013 and 2012, NCDF is servicing \$98,018 and \$150,211 of loans for the KSCR Fund, which is not included in loans receivable.

5. **NOTES PAYABLE**

Notes payable, including accrued interest, are summarized as follows:

	<u>2013</u>	<u>2012</u>
Senior loans payable:		
Institutional	\$ 2,319,445	\$ 2,533,045
Subordinate loans payable:		
Cooperatives	2,851,118	1,613,134
Individuals	562,159	353,513
Institutional	500,014	500,000
Institutional EQ2	1,404,139	1,402,111
	<u>\$ 7,636,875</u>	<u>\$ 6,401,803</u>

(Continued)

NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

NOTES TO FINANCIAL STATEMENTS

For the Years Ended December 31, 2013 and 2012

5. **NOTES PAYABLE (Continued)**

Notes payable at December 31, 2013 have interest rates ranging from 0.25% to 4%, are unsecured, and mature through 2021. Principal maturities of notes payable, including accrued interest, are as follows:

Accrued interest	\$ 179,861
Due on demand – 30 days	213,862
Due on demand – 90 days	868,234
2014	2,269,276
2015	1,064,820
2016	424,762
2017	440,000
2018	751,060
Thereafter	1,425,000
	<u>\$ 7,636,875</u>

6. **LEASE OBLIGATIONS**

NCDF leases its office space under the terms of an operating lease agreement that expires on June 30, 2015. Annual rent is \$9,600.

Rent expense was \$9,200 in 2013 and \$18,038 in 2012. A portion of the rent expense was reimbursed by affiliated organizations through March 31, 2012 (Note 9).

7. **RETIREMENT PLAN**

NCDF has established a salary reduction plan with matching contributions for participating employees. The plan has received IRS approval under Section 408(p) of the Internal Revenue Code. The plan covers all employees who have met certain service requirements. NCDF will match the elective contributions of an employee in an amount not exceeding 3% of the employee's compensation. Matching contributions were \$5,216 for 2013 and \$4,199 for 2012.

8. **STOCKHOLDERS' EQUITY**

**Preferred Stock** - At the discretion of the Board of Directors, NCDF may pay holders of Class A preferred stock an annual dividend of up to 8% in the form of cash, additional shares of Class A preferred stock or equity credits. The Class A preferred stock has no voting rights and shares may only be transferred upon the approval of the Board of Directors. The Class A preferred stock has a liquidation preference over other equity. No dividends were declared or issued during 2013 or 2012.

(Continued)



NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

NOTES TO FINANCIAL STATEMENTS

For the Years Ended December 31, 2013 and 2012

8. **STOCKHOLDERS' EQUITY (Continued)**

Lenders agreed to convert \$55,000 of notes payable into common and preferred stock during 2013.

Pursuant to an exchange agreement, a lender agreed to convert \$500,000 of its outstanding note payable of \$1,000,000 into preferred stock on December 31, 2012. The exchange agreement allows the investor to redeem all or part of its preferred stock under certain conditions on or after April 1, 2021.

**Additional Paid-In Capital** - Additional paid-in capital requirements are determined on a multi-tiered format based on the assets of the member. In April 2012, NCDF amended its requirements for members. Members contributed additional paid-in capital of \$11,245 in 2013 and \$51,030 in 2012 to meet these requirements.

9. **TRANSACTIONS WITH AFFILIATED ORGANIZATIONS**

Several directors of NCDF were employed by, or directors of, NCDF member organizations or other organizations that may be borrowers from, lenders to, or hold common or preferred stock in NCDF. Such activities were in the ordinary course of business at normal credit terms including interest rates and collateralization and do not represent more than a normal risk of collection.

Through June 2012, NCDF was part of the Northcountry family of organizations, which include the Northcountry Cooperative Foundation and Common Properties Management Cooperative. The organizations had an agreement whereby NCDF paid for certain expenses and was reimbursed by these organizations. The agreement was terminated effective June 30, 2012. NCDF was reimbursed \$16,397 in 2012 for occupancy, telephone, computer and office supplies under this agreement.

10. **INCOME TAXES**

NCDF has Federal net operating loss carry forwards of approximately \$1,700,000 that begin to expire in 2027. Minnesota net operating loss carry forwards of approximately \$1,800,000 begin to expire in 2022.

The deferred income tax asset consists of the future tax effect of net operating loss carryforwards and the allowance for loan losses. For financial statement purposes an allowance for loan losses is recorded based on management's review of loans receivable. For income tax purposes, loan losses are deductible when incurred. Deferred tax assets are \$495,000 and \$480,000 at December 31, 2013 and 2012, respectively.

(Continued)

NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

NOTES TO FINANCIAL STATEMENTS

For the Years Ended December 31, 2013 and 2012

10. **INCOME TAXES (Continued)**

Realization of the deferred income tax asset is dependent upon sufficient future taxable income during the net operating loss carry forwards period. Management expects it is more likely than not that a portion of the deferred income tax assets may not be realized, accordingly, a deferred income tax valuation allowance of \$294,800 and \$279,800 has been recorded at December 31, 2013 and 2012. The deferred income tax valuation allowance increased by \$15,000 in 2013 and \$34,000 in 2012.

Utilization of the deferred income tax asset is dependent upon NCDF generating sufficient income within the net operating loss carryforward period. As discussed in Note 11, Management's projection of future income is heavily dependent upon future grant revenues. Due to the uncertainty of future income, it is at least reasonably possible that management's view of future income will change in the near term.

NCDF's provision for income taxes differs from applying the statutory Federal income tax rates to income before income taxes. The primary difference results from the change in the deferred income tax valuation allowance, which was increased in 2013 and 2012 due to the likelihood that NCDF will not generate sufficient taxable income to fully utilize the deferred tax asset.

11. **ACCUMULATED DEFICIT AND MANAGEMENT'S PLANS (Unaudited)**

Loan losses in 2007, 2008 and 2011 related to two cooperative housing development projects created a retained earning (accumulated deficit) in stockholders' equity. Management and the Board are aggressively pursuing a plan to increase stockholders' equity and net income. In 2012-2013, NCDF undertook a capital campaign that:

1. Raised \$641,555 in additional stockholders equity through:
  - a. Conversion of \$550,000 in notes payable to preferred shares in 2012-2013.
  - b. Capital contributions from current members of \$11,245 in 2013 and \$51,030 in 2012.
  - c. Sale of common stock to new members totaling \$19,800 in 2013 and \$9,480 in 2012.
2. Increased interest revenue on loans by \$54,473 from \$431,822 in 2012 to \$486,295 in 2013.
3. Raised \$16,112 in grants in 2013.

(Continued)

NORTHCOUNTRY COOPERATIVE DEVELOPMENT FUND

NOTES TO FINANCIAL STATEMENTS

For the Years Ended December 31, 2013 and 2012

11. **ACCUMULATED DEFICIT AND MANAGEMENT'S PLANS (Unaudited) (Continued)**

In 2014, NCDF will continue the capital campaign and build towards greater profitability and sustainability. Management expects to:

- Increase interest revenue on loans by almost \$28,794 from \$486,295 to \$515,089 through higher lending volume.
- Raise an additional \$500,000 through the sale of preferred shares. An anonymous foundation has pledged up to \$250,000 as a match to preferred stock investments raised in 2013-2014.
- Increase common stock by at least \$16,000 through the sale of common stock to new members and additional capital contributions from current members.
- Obtain \$200,000 in grants, contracts and donations. As of March 31, 2014, NCDF had made significant progress toward that goal with \$115,000 in hand or firmly committed for 2014.

12. **COMMITMENTS**

As of December 31, 2013, NCDF has made commitments of approximately \$658,000 to lend funds in the normal course of business to meet the financing needs of its members. These are commitments to extend credit that involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the financial statements.

13. **SUBSEQUENT EVENTS**

Management has evaluated subsequent events through April 17, 2014, the date on which the financial statements were available for issue, and identified no further significant events or transactions to disclose.